ANNUAL REPORT **2010**

ISAVIA

Airport system 2010

Airports	Movements domestic	Movements international	Passangers domestic	Passangers international
Keflavík	30,475	21,942	–	1,791,143
Reykjavík	62,978	3,360	359,836	41,550
Akureyri	13,556	408	187,749	15,588
Egilsstaðir	3,140	142	89,613	930
Vestmannaeyjar	5,142	–	26,300	–
Bakki	2,002	–	2,211	–
Ísafjörður	2,066	–	43,204	–
Hornafjörður	1,345	–	9,888	–
Sauðárkrókur	862	–	5,979	–
Other airports	3,374	31	13,722	–
Total	**124,940**	**25,883**	**738,502**	**1,849,211**

INTERNATIONAL AIRPORTS
Akureyri, Egilsstaðir, Keflavík, Reykjavík.

OTHER SCEDULE AIRPORTS
Bakki, Bíldudalur, Gjögur, Grímsey, Hornafjörður, Ísafjörður, Sauðárkrókur, Vestmannaeyjar, Vopnafjörður, Þingeyri, Þórshöfn.

OTHER AIRFIELDS AND LANDING GROUNDS
Arngerðareyri, Blönduós, Borgarfjörður eystri, Breiðdalsvík, Búðardalur, Djúpivogur, Fagurhólsmýri, Flúðir, Grímsstaðir, Hella, Herðubreiðarlindir, Hólmavík, Húsafell, Húsavík, Hveravellir, Kaldármelar, Kerlingarfjöll, Kirkjubæjarklaustur, Kópasker, Melgerðismelar, Norðfjörður, Nýidalur, Patreksfjörður, Raufarhöfn, Reykhólar, Reykjahlíð, Reykjanes, Rif, Sandskeið, Siglufjörður, Skálavatn, Skógarsandur, Sprengisandur, Stóri-Kroppur, Stykkishólmur, Vík, Þórsmörk.

CONTENTS

ADDRESS OF THE CHAIRMAN OF THE BOARD OF DIRECTORS

On 29 December 2009, the Icelandic parliament – Althingi – passed Act No. 153/2009 on the merger of the state-owned limited liability companies Flugstodir ltd and Keflavik International Airport ltd into a new private limited liability company which was to assume all the rights and responsibilities of the merged companies as provided for in Act zby the Icelandic Civil Aviation Authority and Act No. 76/2008 on the establishment of a state-owned company for the operation of Keflavik International Airport, etc.

The new company was established on 29 January 2010 with headquarters at Reykjavik Airport. The Minister of Finance is responsible for the state's share in the company and the Minister of the Interior is responsible for strategic planning and technical supervision and for communications with the company with respect to a service agreement with the state.

THE MISSION OF THE COMPANY IS

a. to operate and develop air navigation services, including air traffic control, communications and navigation systems and other related activities

b. to operate and develop airports, property and related activities, including the operation, maintenance and development of Keflavik International Airport as an international civil airport in addition to utilising the airport area for the benefit of security and defence related operations and national obligations

c. to operate, maintain and develop the Leif Eirikson Air Terminal, including the sale of duty free goods in the airport area

d. to manage business directly involving aircraft operation, operation of airports and air terminals and other operations within the Airport Security Restricted Area

e. to exercise the rights and meet the obligations of the Icelandic state pursuant to international conventions and agreements or agreements with other states including international aviation services

The company may enter into the establishment of other companies and enterprises, and obtain part in other companies and enterprises, including a company intended to manage the industrial development of the surroundings of Keflavik International Airport. The company may also enter into any kind of agreement with other parties in order to achieve its purpose in the most efficient manner.

The company is directed by a seven-member Board of Directors with seven alternates. The board directors are: Ms Arnbjorg Sveinsdottir, Municipal Representative and alternate Member of Parliament; Mr Arngrimur Johannsson, Flight Captain; Ms Asta Rut Jonasdottir, Business Administrator; Mr Jon Nordfjord, Managing Director; Ms Rannveig Gudmundsdottir, former Member of Parliament and Minister; Mr Ragnar Oskarsson, Upper Secondary School Teacher; and Mr Thorolfur Arnason, Engineer.

Alternate board directors: Mr Asgeir Magnusson, Ms Gudny Maria Johannsdottir, Mr Hjortur M. Gudbjartsson, Mr. Jonas Bjarnason, Ms Margret Kristmannsdottir, Mr Olafur Sveinsson and Ms Sigrun Palsdottir.

In its first meeting, the board members assigned tasks among themselves and elected Mr Thorolfur Arnason as Chairman and Ms. Rannveig Gudmundsdottir as Vice-Chairman. Mr Bjorn Oli Hauksson, Managing Director of Keflavik International Airport ltd, was appointed Managing Director of the company on 1 May 2010 when Isavia ltd formally took over the operation of Flugstodir ltd and Keflavik International Airport ltd.

At the follow-up founding meeting on 29 April 2010, Ms Dagny Halldorsdottir and Ms Johanna Harpa Arnadottir were elected alternate members of the Board, replacing Ms Gudny Maria Johannsdottir and Ms Margret Kristmannsdottir. The follow-up meeting also approved the proposal to name the company 'Isavia' which was previously used by Flugstodir ltd internationally.

The Board has conducted 20 meetings since the company was established, thereof 16 in 2010. The Board's regular meetings are held on the last Thursday of each month. Alternates were specifically asked to attend the December meeting when the company's operating budget for 2011 was discussed.

The Board is resolved to visit the company's principal operating units at regular intervals and to conduct board meetings at those different locations in Iceland. A board meeting was held in Akureyri on 26 March 2010, in Egilsstadir on 1 October 2010 and in Vestman Islands on 1 April 2011. This arrangement has been a great success. The Board has met with local employees and has had the opportunity of gaining a clearer picture of the operation than would otherwise have been the case. Board meetings are in other respects held alternately in the company's main offices at Reykjavik Airport and at Keflavik Airport

MAIN TASKS OF THE BOARD:

Preparations for the merger of Flugstodir and Keflavik International Airport into a new limited company were by far the largest task undertaken by the Board during the first year of operation. Three months elapsed from the founding of the company until the companies were merged into Isavia. During this period Mr Thorolfur Arnason was hired temporarily to manage the merger.

Although various issues arose during the implementation of the merger, Isavia's Board is of the opinion that the merger of Flugstodir ltd and Keflavik International Airport ltd into Isavia ltd has been a great success.

The 2010 operating results of the merged company are better than predicted. All key managerial positions have been filled in accordance with the new organisational chart which came into effect in September 2010. All the company's tasks have been performed in accordance with the strict security requirements that apply, and the company's activities that are subject to licencing have progressed smoothly. All necessary operating licences and airport certificates were ready when the merger was implemented; their issue by the Civil Aviation Authority is a prerequisite for the company's operation of airports and air navigation services. The volcanic eruption in Eyjafjallajokull volcano, which began just prior to the merger, showed the strength of the new company clearly and memorably. The future employees of the new company tackled unprecedented conditions in aviation operations and did their jobs exceptionally well. In a way, this natural disaster brought the team together, created a strong spirit and was in fact a true baptism of fire.

AUDIT OF THE MERGER

The National Audit Office performed an administrative audit on the merger of the companies that was published in October 2010. The Audit Office was of the opinion that the merger was a successful venture on the whole, but a few issues that could have been improved were identified.

FINANCES

Monitoring the finances of a limited company is always the most important task of the board of directors. Key figures in Isavia's finances from the previous month's operating results are reviewed at each meeting, as are individual issues that require resolution and the involvement of the Board. Difficult circumstances surrounding State finances have impelled the owner of the company (the State) to reduce contributions and to levy taxes on the business which the company has had to meet by raising user fees and increasing economisation. The company's operation is stable, although capital formation is insufficient to cover necessary renewals of airport installations and air navigation systems for the future. The company's main task over the next few years will be to ensure sufficient funds for investment. Isavia, however, is not the only state-owned company dealing with this problem as a result of the current difficult economic circumstances. Building up the company's finances will take a long time. Nevertheless, the course has been set and the company will continue undaunted to build a strong and dynamic airport operation and air navigation service company.

POLICY FORMULATION

Policy formulation for the new company began as early as May last year. The role of the company, its values and its future vision were examined closely. The Board and employees embarked on this work under the guidance of experts from the company Expectus, and had more or less completed the basic work by August 2010. The company's values are safety, co-operation and service. The role of the company is as follows: "We provide aircraft operators and other entities that require access to airports, our customers and their customers with safe and convenient airports, air navigation services and related activities. Our services aim to be safe, economical and of the highest quality in an international context". Work continued in separate work meetings of individual operating units. The policy is at present being systematically implemented within the company. One aspect of the company's policy formulation was a decision to enrol the company into the Travel Industry Association which is a member of the Confederation of Icelandic Employers. This underlines the fact that the company is part of the Icelandic travel sector, and at the time of writing it was the second largest member of the Travel Industry Association.

EQUAL RIGHTS PROGRAMME

The company has established an equal rights policy and an ambitious equal rights programme. Its object is to ensure full equality of men and women in the company's workplaces with the goal of taking advantage of staff abilities, energy and knowledge, free of gender-based discrimination.

It is the opinion of the Board that the establishment of Isavia and the merger of Flugstodir and Keflavik International Airport were successful. It is also safe to say that the operation of the company in 2010 exceeded our expectations when taking into account the numerous issues that were working against it. On the whole, the company has a bright future ahead.

On behalf of the Board of Isavia ltd,

Thorolfur Arnason, Chairman

Board of Directors of Isavia, upper row from left to right: Bjorn Oli Hauksson, Arngrimur Johannsson, Arnbjörg Sveinsdottir, Ragnar Oskarsson, Jon Nordfjörd. Lower row from left to right: Asta Rut Jonasdottir, Thorolfur Arnason, Rannveig Gudmundsdóttir.

VOLCANIC ERUPTION IN THE EYJAFJALLAJOKULL GLACIER

The volcanic eruption of Eyjafjallajokull glacier had a considerable impact on Isavia's operations in the company's first year. Company employees tackled unprecedented conditions and resolved the issues that arose exceptionally well during the eruption. International flights had to be re-routed from Keflavik Airport to Akureyri and Egilsstadir, and there was a huge increase in traffic through the Icelandic air traffic control area as the eruption progressed.

VOLCANIC ERUPTION IN THE EYJAFJALLAJOKULL GLACIER

The volcanic eruption of Eyjafjallajokull glacier caused considerable disruption of international flights to and from Iceland. It is safe to say that the actions taken to secure flights to and from Iceland during the eruption were successful. The ash from Eyjafjallajokull affected both international flights to Iceland and also air traffic through the Icelandic air traffic control area. The volcanic eruption had an impact on a large number of Isavia employees, and everyone involved worked selflessly to ensure that as the situation was resolved as smoothly as possible. Flugstodir and Keflavik International Airport employees, now working together under the banner of Isavia, began their partnership in a most memorable fashion.

Many journalist from the international media who contacted Isavia during the eruption were quite astonished to learn that operations continued uninterrupted at Icelandic airports while air traffic on mainland Europe was severely disrupted as a result of the eruption.

The Icelandic international airports were only closed simultaneously for a few hours during the entire period of volcanic activity.

Akureyri International Airport was very busy during the period of 22 – 29 April and 8 – 14 May when several B-757 and B-737 were sometimes being serviced at the same time at the airport.

The swift transfer of all international operations to Akureyri required great ingenuity. For example, an improvised lounge was set up in an aircraft hangar for waiting passengers.

APRIL

14 APRIL The volcanic eruption of Eyjafjallajökull began in the morning of 14 April. The volcanic ash had a serious impact on air traffic in northern Europe. The ash did not have affect the status of airports in Iceland at first.

16 APRIL On 16 April, the preparation of a response plan began which was intended to ensure increased resources and facilities to enable the transfer of international flights from Keflavik to Akureyri and Egilsstadir.

22 APRIL It was not until 22 April that international flights were transferred from Keflavik Airport to Akureyri and Egilsstadir. This transfer was achieved in a very short space of time through the co-ordinated efforts of many parties. This period lasted until 29 April.

Keflavik International was closed for parts of 10 days during the eruption, and not in sequence.

Each time that airborne volcanic ash threatened to close Keflavik International, a combined operations centre of Icelandair and Isavia was activated at Reykjavik Airport to ensure co-ordination of control and activities of all operators.

A total of 48 flights carrying 9,639 passengers went through Akureyri International in the time that Akureyri served as primary International Airport in Iceland. Many of the airport staff assumed new and unusual roles during this trying time in order to maintain uninterrupted international operation.

VESTMANNAEYJAR AIRPORT

Check-in operations were expedient, but waiting lines were unavoidable due to limited capacity at small the terminal.

Egilsstadir International was also used during the eruption, however much less than Akureyri due to the distance from Reykjavik. Five passenger jets went through the airport.

In early May, nearly all transatlantic airline traffic that normally passes through four different air traffic control areas was routed through the Icelandic area.

MAY

7 MAY On 7 May, the direction of winds in the upper atmosphere changed. This lead to changes in ash dispersion from the volcano. As a consequence almost all air traffic over the North Atlantic Ocean was routed through the Icelandic air traffic control area. Air traffic records were broken four times during a five-day period.

8 MAY The next day, 8 May, international flights were transferred back to Keflavik Airport. This period ended on 14 May.

Flights in Iceland had for the most part returned to normal by the end of May.

The Executive Board of Isavia: From left to right: Hjordis Gudmundsdottir, Haukur Hauksson, Hlynur Sigurdsson, Helga R. Eyjolfsdottir, Asgeir Palsson, Omar Sveinsson, Stefan Jonsson, Sigurdur Olafsson, Bjorn Oli Hauksson, Fridthor Eydal, Ingunn Olafsdottir and Elin Arnadottir.

MERGER OF FLUGSTODIR LTD AND KEFLAVIK INTERNATIONAL AIRPORT LTD

On 1 May 2010, the state-owned limited liability companies Flugstodir and Keflavik International Airport merged into a single company named Isavia ltd.

Flugstodir, in operation since the beginning of 2007, was responsible for the operation and development of all airports and airfields in Iceland, with the exception of Keflavik International Airport, together with the air navigation services that Iceland provides for domestic and international flights. Keflavik International Airport ltd was founded at the beginning of 2009 to oversee the operation, maintenance and development of the airport and its terminal, the provision of services for flight operators and utilisation of the airport for national security and defence operations.

The merger the two companies laid the foundation for new aviation and business operations and services. The Minister of Finance is responsible for the State's share in the company, while the Minister of the Interior is responsible for strategic planning and technical supervision.

On the merger of the companies, Mr. Thorgeir Palsson Managing Director of Flugstodir retired and Bjorn Oli Hauksson, business engineer and former Managing Director of Keflavik International Airport, was appointed Managing Director of the new company.

The first year of operation has been characterised by extensive work on the merger and redefinition and unifying of tasks.

The IT systems of the companies differed considerably, and user rules, security, human resources systems, time recording and wage systems needed to be unified. Work was also carried out on the unification of various operating procedures and work practices.

A few days before the merger, a volcanic eruption began on the Eyjafjallajokull Glacier which had a considerable impact on the operations of both Flugstodir and Keflavik International. One could say that the merger of the companies went off with a bang. An effective operations control was established swiftly with representatives from all principal stakeholders to conduct operations that aimed at maintaining uninterrupted air transport services.

DIRECTOR'S OFFICE

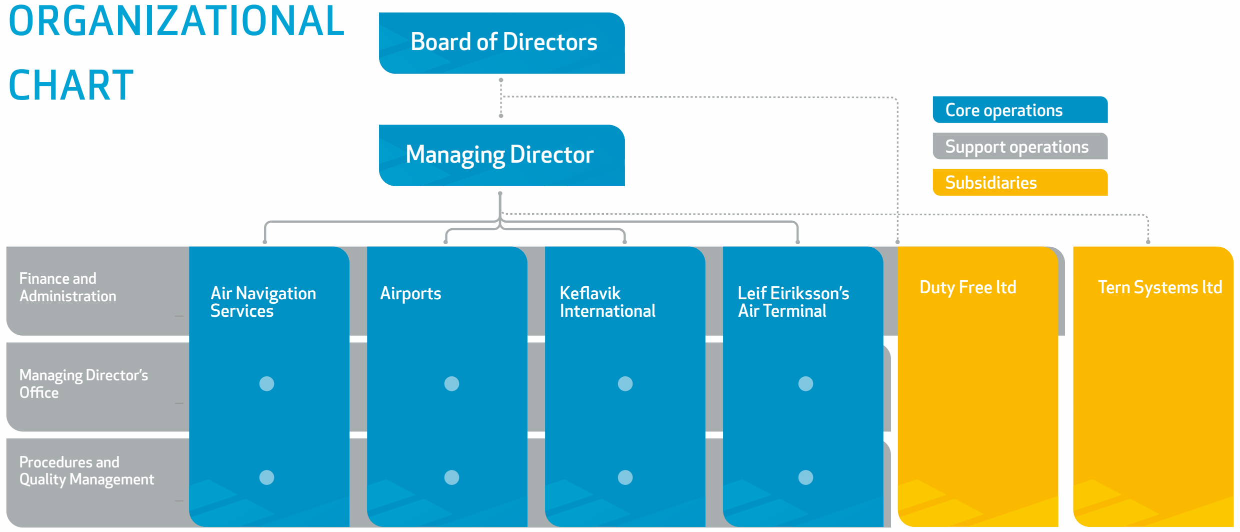
The Director's Office was established to provide policy and co-ordination support to the Board of Directors, Managing Director and operating units of the company in the fields of legal affairs, government relations, contracting and international research and development. The office oversees co-ordination and policymaking concerning airport services and security, zoning and development, municipality relations and provides support and administration for the board of directors of Isavia ltd, The Duty free Store ltd and Tern ltd. The Director's Office is also responsible for service contracts, defence programs, corporate communications and public relations, publication, websites and company files.

The Procedures and Quality Manager operates in close co-ordination with the Director's Office. The separate operating licences of Flugstodir and Keflavik International Airport for air navigation services were merged into one, and individual operation certificates for the airports were re-issued by the Iceland Civil Aviation Authority. Operational systems and procedures were co-ordinated in air navigation services, airport operations and quality and safety management so as facilities, equipment and staff performance comply with national and international standards and obligations. The quality and safety management system is designed in accordance with the ISO 9001 standard.

ISAVIA'S ROLE

Isavia ltd is the national operator of all airports and air navigation services in Iceland that cover approximately 5 million square kilometres. The company ensures aviation safety and airport security in accordance with recognised international security requirements and methods. Isavia and its subsidiaries had an average of 660 full time employees with a surge of 870 during the summer of 2010. The company places emphasis on maintaining a team of highly-skilled professionals. The operation is supervised by the Icelandic Civil Aviation Authority in accordance with operating licences issued by the ICAA.

ORGANIZATIONAL CHART



KEY FIGURES

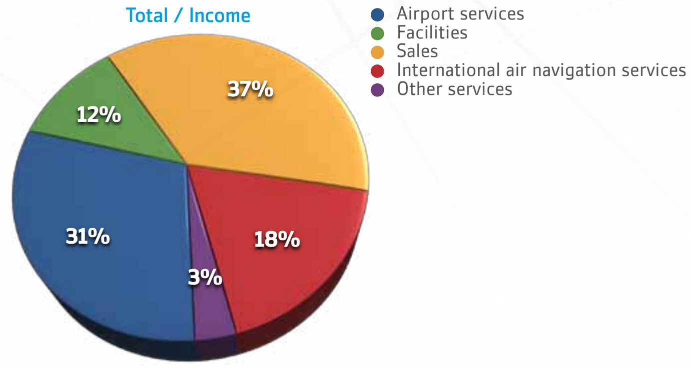
FROM THE CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME	
Revenue	14.136
EBITDA	3.045
EBIT	1.723
Financial income/expenses	843
Profit before taxes	2.567
Operating profits	2.125

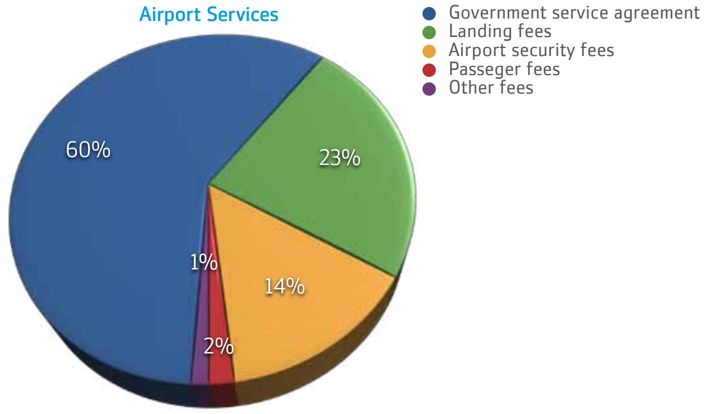
FROM THE CONSOLIDATED STATEMENT OF FINANCIAL POSITIONI	
Property, plant, and equipment	22.017
Assets	32.069
Equity	10.302
Interest bearing liabilities	18.348
Current ratio	1,01

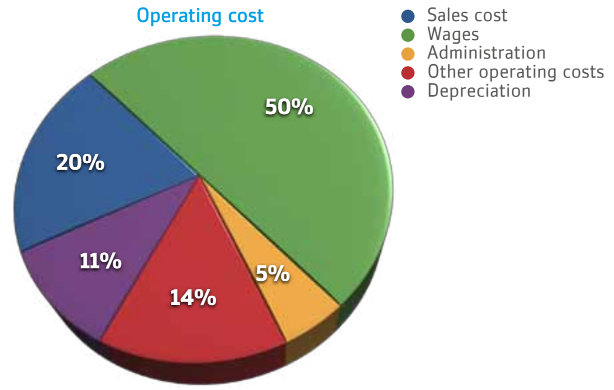
FROM THE CONSOLIDATED STATEMENT OF CASH FLOWS	
Operating activities	1.590
Investing activities	-715
Financing activities	-1.247
Cash and cash equivalents at end of the period	1.506

FINANCIAL INDICATORS	
Contribution margin on operation	22%
Profit margin on operating revenue	15%
Rate of return on assets	0,43
Return on equity	23%
Earnings per share	0,38
Equity ratio	32%

Amounts in ISK millions







FINANCIAL HIGHLIGHTS

The 2010 Consolidated Financial Statements of Isavia have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU). Keflavik International Airport published its financial statements in the same manner while Flugstodir did not.

The company was established with ISK 10m in shares. The establishment capital from Flugstodir was ISK 2.4bn and ISK 5.9bn from Keflavik Airport. Changes due to the adoption of IFRS meant that equity had to be reduced by ISK 260m. For the most part, this involved the reduction of intangible assets which were not regarded as assets according to international financial reporting standards.

According to the Consolidated Statement of Comprehensive Income, the company's 2010 operating revenues amounted to ISK 14,136m. Profits for the year amounted to approximately ISK 2,125m. According to the balance sheet, the Group's total assets amount to approximately ISK 32,069m. Recorded equity at year-end 2010 amounted to approximately ISK 10,302m and the company's equity ratio was 32%.

The operating income of Isavia and its subsidiaries consists of airline operatpr charges, including communication charges, airspace charges, landing and passenger charges, property rental and income from operating permits together with retail income. Income from air navigation services within the Icelandic flight information region and a proportion of the flight information region of Greenland and the Faroe Islands amounts to approximately 18% of total income. Service revenues from Icelandic airports form approximately 31% of the company's total income. Keflavik International Airport, Reykjavik Airport, Akureyri Airport and Egilsstadir Airport are the largest airports. Income derived from the service agreement with the Ministry of the Interior amounted to ISK 2.5m in 2010. Income from retail sales is approximately 37% of total income, making it clear that the operation of the Duty Free Store in the Leif Eiriksson Air Terminal is a very important source of income. Other income includes property income from the lease of facilities at the airport, software sales, income from Isavia's involvement in overseas projects, services sold, etc.

Operating expenses excluding depreciation and financial items amounted to ISK 11,092m, whereof the cost sales amounted to ISK 2,503m, which was 47.43% of the company's goods sales. Payroll expenses were ISK 6,194m, approximately 43% of total income. The average number of full-time equivalent positions in 2010 was 707. Other operating expenses amounted to ISK 1,777m, and administrative costs were ISK 618m. This includes costs resulting from the merger, approximately ISK 60m. The merger, restraint and cost consciousness characterised the company's operation in 2010, although activities in relation to the volcanic eruption of Eyjafjallajokull in the spring resulted in increased costs due to the transfer of all flights to Akureyri when Keflavik Airport closed for a period. The company's costs, taking into account lost income and communication charges during the eruption, are estimated to be approximately ISK 120m.

Net income before depreciation and financial items was approximately ISK 3,045m, resulting in a contribution margin of approximately 27%. The contribution margin needs to be between 25% and 30% if the operation of the group is to be sustainable based on the current capital structuring. The company's depreciation amounts to approximately ISK 1,321m whereof intangible assets, that is, the company's entitlement to use airfield facilities and items of equipment that are a part of the NATO Security Investment Programme funded installations, are ISK 206 million. The company's principal assets consist of the Leif Eiriksson Air Terminal, the air traffic control centre and control tower at Reykjavik Airport and the telecommunications centre at Gufunes. Moreover, the company owns real property alongside the Haaleiti apron at Keflavik Airport. Depreciation of real property amounts to ISK 466m. The book value of control systems, approach equipment and other property, including vehicles, fire engines, machinery and other equipment relating to airport operation together with telecommunications equipment in various parts of Iceland, is estimated to be approximately ISK 3.8bn.

Financial items are positive by approximately ISK 843m, whereof interest income is ISK 219m. Interest costs on long-term loans amount to ISK 774m. The average interest rate on the company's current debt portfolio is approximately 3.3%. There were considerable fluctuations in the exchange rate of the Icelandic krona during the year, resulting in foreign currency gains amounting to approximately ISK 1,399m. The company's profit before taxes amounted to ISK 2,567m. No income tax will be paid in 2010 due to the accrued losses of previous years. The calculated income tax amounts to ISK 442m. The company's total profits, therefore, were positive by ISK 2,125m in 2010.

As in the three years prior to 2010, the year was characterised by considerable restraint in investments. Embarking on a number of investments and larger maintenance projects, such as increasing the number of aprons at the Leif Eiriksson Air Terminal, has become very urgent. Investments in 2010 amounted to ISK 704m. The company estimates that investments amounting to ISK 1,6bn will be required to maintain the capital bound in Isavia's operations. Financing activities were ISK 1,247m whereof instalments on long-term debts amounted to ISK 1,237m. Net cash from operations in the company's opening balance sheet was ISK 1,895 million. Net cash from operations was ISK 371 million lower at year-end than at the beginning of the year.

The book value of the total assets of Isavia at year-end 2010 was ISK 32,069m, of which fixed assets accounted for ISK 28,660m. The company's net liabilities, i.e. liabilities less current assets, were approximately ISK 18,358m. Loans were paid off to the amount of ISK 1,247m. Moreover, the strengthening of the Icelandic krona reduced the company's debt position by approximately ISK 1,269m in 2010. Current maturities of long-term loans amount to around ISK 1,357m. The company's equity has increased by approximately ISK 2,179m since its establishment and its equity ratio at year-end 2010 was 32% as compared to 24.6% on its establishment.

AVIATION IN ICELAND 2010

TRAFFIC IN THE ICELAND AIR TRAFFIC CONTROL AREA

Air traffic through the Iceland Air Control Area increased by 0.8 per cent in 2010 compared to the previous year. A total of 102,275 aircraft flew through the area, an average of 280 per day. The corresponding number in 2009 was 101,503. The greatest volume of traffic during a single month was in July, when over 11,600 aircraft flew through Icelandic airspace, an average of 375 per day. The greatest number of aircraft in a single day was on 11 May, when 1,019 aircraft passed through the area. There was a decrease during the first few months of the year due to the eruption of the Eyjafjallajokull volcano. The greatest decrease was in April with a reduction of 27 per cent compared to the same month in the preceding year. Approximately 25 per cent of the air traffic was en route to or from Iceland, a similar proportion as in the year before.

AIRCRAFT MOVEMENTS PASSENGERS, DOMESTIC FLIGHTS

The total number of passengers at Icelandic domestic airports fell by approximately 9.4 per cent in 2010, from 815,042 to 738,502. Each passenger on domestic flights is counted twice, on departure and arrival. Passengers increased by 2 per cent in Akureyri while decreasing elsewhere. The greatest decrease was at Bakki, 87.7 per cent and in Vestman Islands, 52.5 per cent. The largest number of domestic passengers goes through Reykjavik Airport, 48.7 per cent, while 25.4 per cent pass through Akureyri, 12.1 per cent through Egilsstadir, 5.9 per cent through Isafjordur and 3.6 per cent through Vestman Islands Airport. Other airports have less than 2 per cent share. Following the opening of a new ferry harbour at Landeyjar, the government stopped subsidising flights between the mainland and Vestman Islands which led to decreased seat availability which is the main reason for the substantial decrease in air passengers on that route.

PASSENGERS, INTERNATIONAL FLIGHTS

The number of passengers on international flights rose by 8.9 per cent during the year, from 1,697,888 to 1,846,211. By far the largest proportion of international passenger throughput is at Keflavik Airport, 96.9 per cent. Reykjavik Airport is in second place with 2.2 per cent, then Akureyri with 0.8 per cent and thereafter Egilsstadir with 0.1 per cent. Of the individual airports, the greatest proportional increase was at Akureyri with 135.8 per cent. This was due to the temporary closure of Keflavik Airport following the volcanic eruption in April and May.

TRAFFIC AT KEFLAVIK AIRPORT

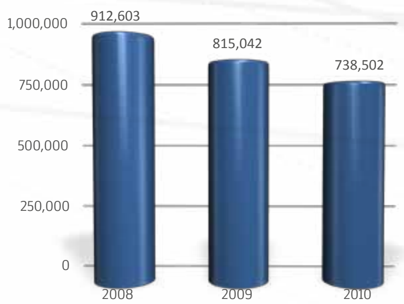
Despite disruptions to air traffic in the spring months as a result of the volcanic eruption, the total number of passengers increased during the year, with 1,791,000 passengers passing through Keflavik Airport. This corresponds to an increase of 8 per cent from last year. The greatest increase, 38.9 per cent, was in transit passengers – passengers who have a short stop in Iceland while travelling between America and Europe. The proportion of transit passengers as a share of the total rose from 14 per cent in 2009 to 18 per cent in 2010. Arrival passengers increased from 706,000 to 718,000, approximately 1.7 per cent, while departure passengers increased from 715,000 to 743,000, approximately 4 per cent.

According to head counts performed by the Iceland Tourist Board at Keflavik Airport, the number of Icelandic departure passengers increased by 15.4 per cent between years, rising from 255,000 in 2009 to 294,000 in 2010. At the same time, the number of foreign departure passengers fell by 1 per cent, from 465,000 in 2009 to 459,000 in 2010.

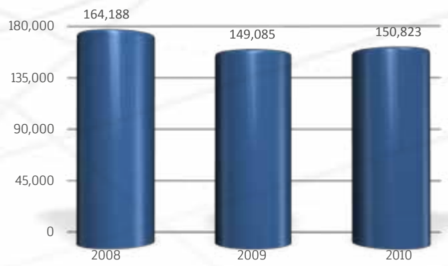
Several new flight destinations were added during the year. Iceland Express began flying four times a week to New York and twice a week to Winnipeg in Canada during the summer months. This was the first time that the company offered flights to destinations outside Europe and used Keflavik International as a hub for transatlantic flights similar to Icelandair. Icelandair began flying twice a week to Trondheim, while Brussels in Belgium became a new destination in the company's route system which, in 2010, consisted of a total of 26 destinations. In addition to new destinations, there was an increase in the frequency of flights to some destinations. New destinations in Europe offered by Iceland Express during the year included weekly flights to Milano Bergamo and flights twice a week to Luxemburg. SAS offered scheduled flights to Oslo throughout the year, and several new airlines began flying to Iceland during the year. Transavia France from Paris Orly over the summer months, and Air Greenland offered flights from Nuuk and Narssarsuaq. Air Berlin, Germanwings, and Lufthansa also offered flights to Iceland in their summer schedules and some overseas airlines offered charter flights.

FLIGHT STATISTICS

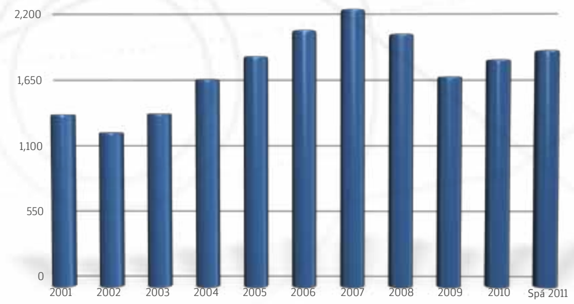
Domestic Passegers



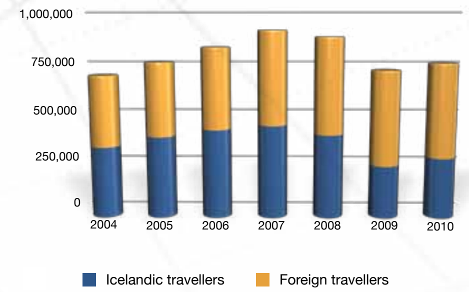
Domestic Airport Movements



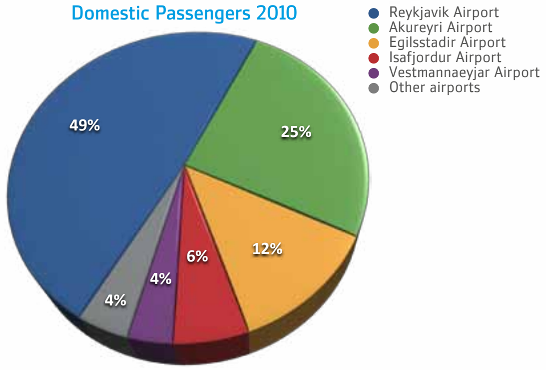
Passengers – Keflavik



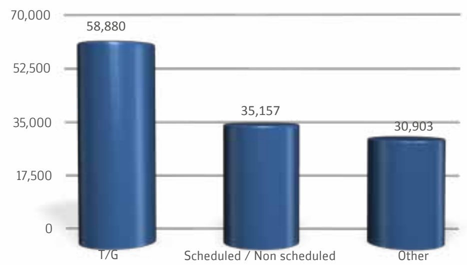
Departure Passegers – Keflavik



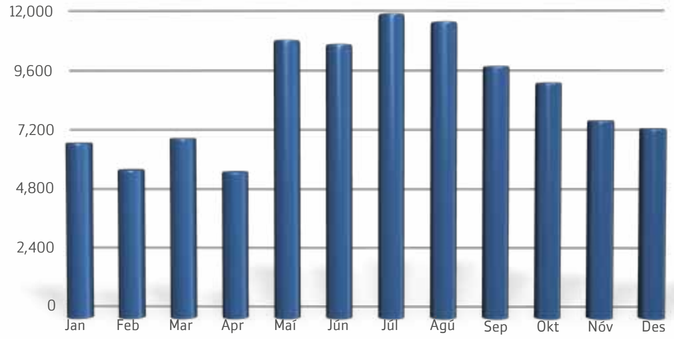
Domestic Passengers 2010



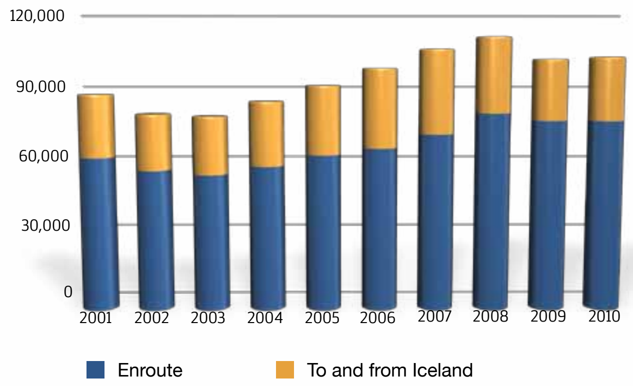
Domestic Flight Movements by Type



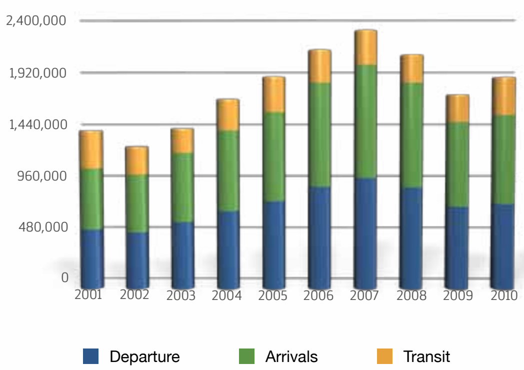
Air Traffic in the Icelandic ATC Area 2010



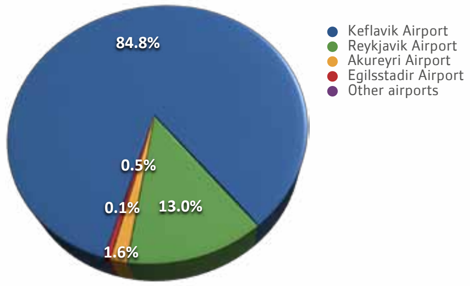
Traffic in the Icelandic ATC Area – Development

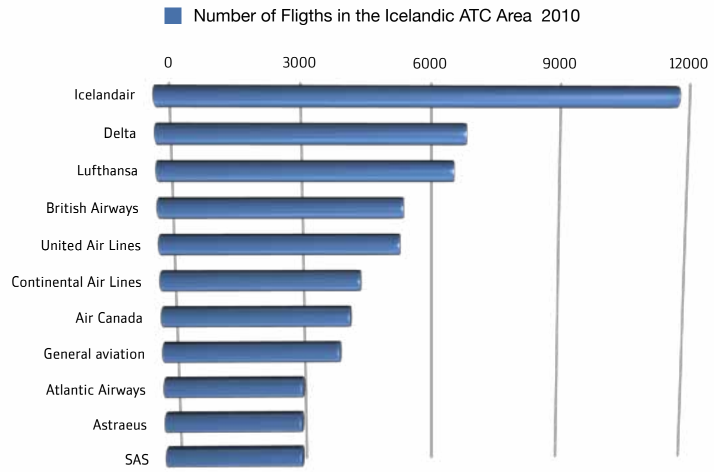


International Passengers

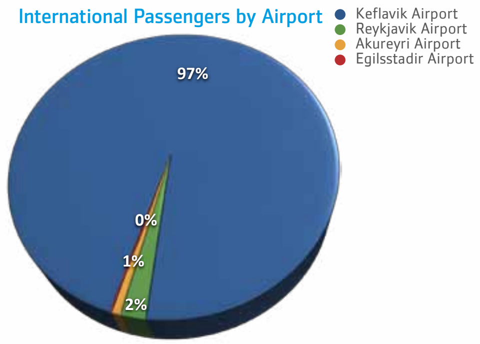


International Airport Movements





International Passengers by Airport



FINANCE

The unification of accounting, purchasing and financial procedures was a major task during the year. A new accounting system was installed with the view of making it easier to analyse the scope of activities in individual departments within the company. The adoption of new procedures for purchasing processes proceeded during the year and involved monitoring and the overall management of tenders and negotiations for larger purchases, as well as communications with service entities, suppliers and the State Trading Centre.

Isavia's financial statements are governed by a variety of rules such as the Joint Finance Agreement with the International Civil Aviation Organization, rules on the transparency of fees at Keflavik Airport and provisions contained in the company's service agreement with the Ministry of the Interior to the effect that it must be possible to analyse individual units within the agreement.

Finance and Administration Division, provides support to the operating divisions of Isavia and to the Duty Free Store. Ms Elin Arnadottir is the director of the division.

FINANCIAL STATEMENTS

The Board decided that the company's financial statements should be prepared in accordance with International Financial Recording Standards (IFRS), which in turn were adopted in the company's Q2 statements. The Board also decided that Isavia's subsidiary, Gannet ltd (Flugfjarskipti), should merge with Isavia as of 1 July 2011, and that the company's statements should be prepared in accordance with the then applicable accounting base. The company's accounts and employees were transferred to Isavia on 1 January 2011.

CHARGES SCHEDULES

A revision of the airport charges schedule for Keflavik International Airport took place in mid- 2010, in line with ICAO policies, EU Council Directives and the Aviation Act, which stipulate that charges shall support the operation of the airport and air navigation services. This was done due to planned changes to the funding of the National Transport Plan, which provides for the discontinuation of airport taxes and alternate airport charges and their replacement by airport service fees. At the same time, work was carried out on a cost analysis of the domestic airports system, and discussions were initiated with the Ministry of the Interior concerning extensive cuts in contributions to the company on the basis of the service agreement although no changes have been made to the required level of service. Meetings were also held with users of Keflavik Airport and the domestic system as stipulated by regulations.

BUSINESS DEVELOPMENT

The company explored ways to increase the number of tourists to Iceland with emphasis on the off-season and winter months. International conventions of airports and airline operators were attended and an incentive program in connection with new destinations was started. Isavia also initiated a special marketing campaign for direct international flights to Akureyri and Egilsstadir in co-operation with regional marketing offices and the local municipalities. A good co-operation has also been with Promote Iceland which has taken part in this important program.

VALUE

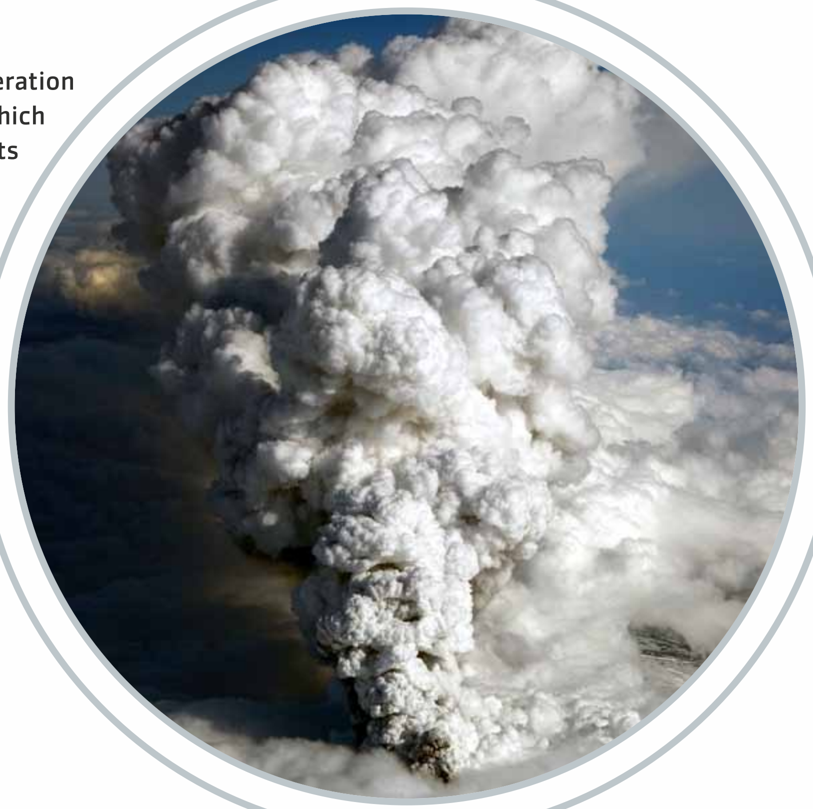
CO-OPERATION

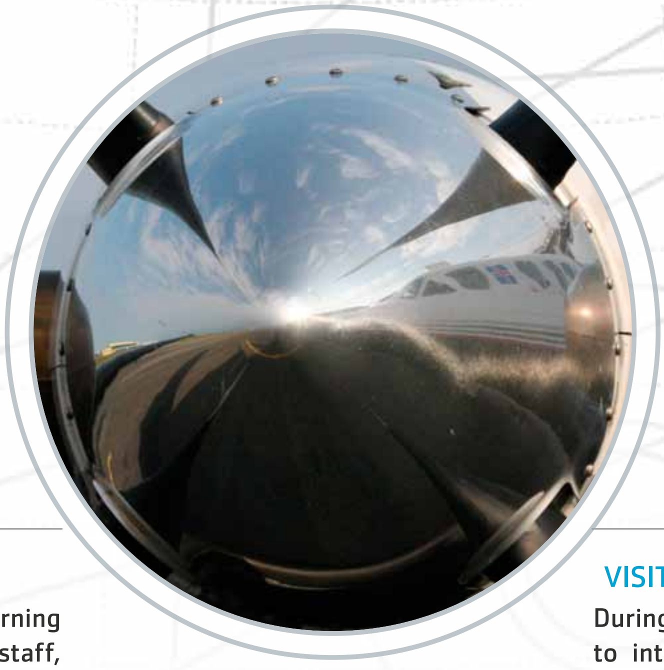
We establish clear service benchmarks and greet our customers with positive attitude and respect.

We exercise prudence and seek ways to maximise success.

EMPLOYEE SERVICES

Isavia is a member of the Confederation of Icelandic Employers, which negotiates wage contracts on its behalf. The employees belong to 28 different trade unions in various parts Iceland, and all collective wage agreements became due for renegotiation during the year. Collective wage agreements to which Isavia was a direct party were negotiated in mid-year. However, the operating position of the company and operating circumstances do not yet give much scope for wage changes.





The company's total staff turnover during the year was just under 8 per cent. The actual turnover was 4 per cent when those who retired or those whose employment was terminated are excluded. The number of employees at year end totalled 546. The Employee Service also provides support to the Duty Free Store which had 108 employees at the end of the year.

The unification of services and procedures was a principal task during the year. Isavia has established the values safety, service and co-operation, and the company bases its human resources policy on these values. In addition to professional ability, Isavia requires an aptitude for service, security consciousness and skill in communication and co-operation when selecting staff.

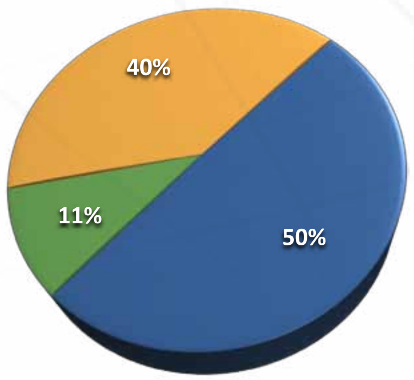
The company's code of ethics provides guidance on how employees should communicate and interact with customers. Isavia has also formulated policies on equality in accordance with legislation on the equal rights of men and women to work. The company focuses on providing employees with equal rights and equal opportunities to benefit from their own merit and develop their talents.

EDUCATION AND TRAINING

Basic education, continuous learning and vocational training for staff, designed among other things to maintain certification, plays a large role in the company's operations. A total of 556 employees completed courses or training in the company school or on contracted courses. Approximately 34,000 working hours were spent on training and education during the year. This is equivalent to 17 employees being in continuous training for the entire year. This does not include the time spent by company staff providing training instruction. The company is also responsible for extensive training for other companies and training of individuals who work in or are authorised to enter airport security areas. In addition, The Isavia School is a generic term that spans all the extensive activities in which the company is involved in the field of training and education.

VISITS

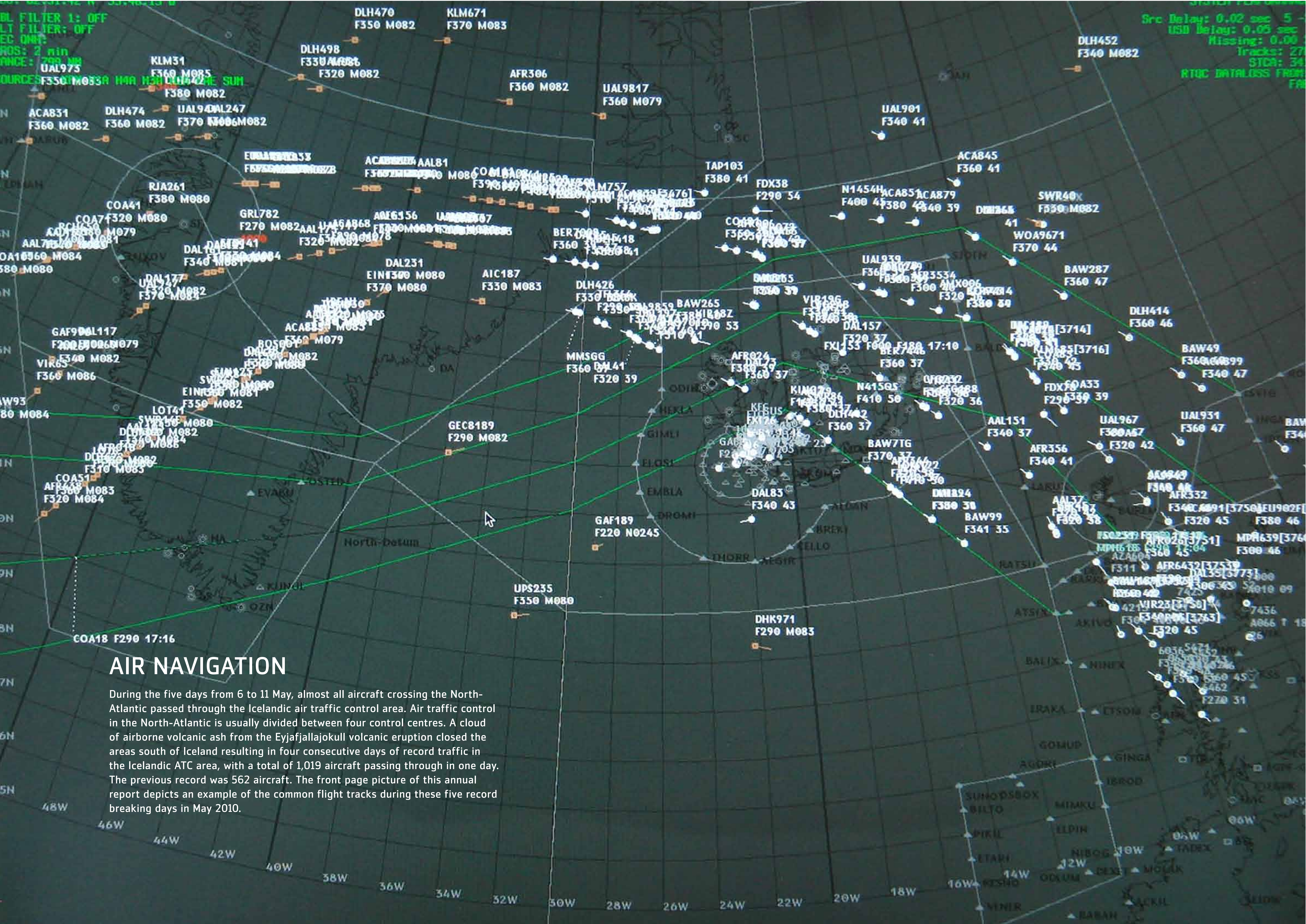
During the autumn, an effort was made to introduce employees to each other's workplaces. Staff in Reykjavik was invited to visit and acquaint themselves with operations at Keflavik International Airport and in the Leif Eiriksson Air Terminal. Similarly, the Keflavik staff toured the company headquarters in Reykjavik, the air traffic control centre, airfield services and flight control tower. The staff associations organised a joint summer outing and are currently involved in cementing co-operation and eventual unification.



HEALTH AND SAFETY

A prerequisite for enabling the company to offer its customers the best available service is ensuring that employees feel secure and content in their jobs. The company attaches considerable importance to providing a beneficial working environment and ensuring that employees are aware of what is required of them with regards to occupational health and safety regulations.

The company focuses on employee health and encourages regular physical exercise in addition to regularly monitoring the health of certain professions



AIR NAVIGATION

During the five days from 6 to 11 May, almost all aircraft crossing the North-Atlantic passed through the Icelandic air traffic control area. Air traffic control in the North-Atlantic is usually divided between four control centres. A cloud of airborne volcanic ash from the Eyjafjallajokull volcanic eruption closed the areas south of Iceland resulting in four consecutive days of record traffic in the Icelandic ATC area, with a total of 1,019 aircraft passing through in one day. The previous record was 562 aircraft. The front page picture of this annual report depicts an example of the common flight tracks during these five record breaking days in May 2010.

AIR NAVIGATION SERVICES

The year 2010 was a year of considerable change in the organisation of air navigation. Before the merger of the two companies, Keflavik International Airport and Flugstodir operated two separate air navigation services. At Flugstodir, the service belonged to two different operating fields, the Air Traffic Control division and the Airport and Air Navigation division and the subsidiary Gannet ltd.

This arrangement remained for the most part unchanged until all Isavia air navigation services were merged on 25 October 2010 on the establishment of the company's new Air Navigation Division. The subsidiary company, Gannet, subsequently merged with the Air Navigation Services Division on 1 January 2011. This united all air navigation services and its operating permit issues under a single management. The Director of the Air Navigation Services Division is Mr. Asgeir Palsson.

The eruption of the Eyjafallajokull volcano set its mark on the operation of the division during the year. Employees worked under considerable strain, particularly near the end of the eruption when almost all air traffic over the North Atlantic was routed through the northern part of the Icelandic air traffic control sector. Traffic records were broken four times during that period.

THE AIR NAVIGATION SERVICES DIVISION TECHNICAL SERVICES

Extensive safety requirements are imposed on air navigation services. Projects relating to improvements and adaptations of systems and equipment in air traffic control and communications centres are continuously underway.

A new air navigation positioning system was implemented in the flight information regions in Reykjavik and Kangerlussuaq (Søndre Strømfjord) in Greenland. This technology is named ADS-B (Automatic Dependent Surveillance – Broadcast) and is based on transmissions from the positioning systems of individual aircraft to air control centres. The system is expected to be ready for trial operation at the end of 2011.

The adoption of a new air traffic control system for the processing of radar data and flight information is also under way at Keflavik International Airport.

The air navigation equipment at Akureyri Airport was updated during the year with new ILS localiser and glide path transmitters installed for runway 01. This means that there are now two separate approach tracks for this runway.

The design of the AMHS message relay system was completed during the year. Over the next few years, this system will replace the traditional AFTN/CIDIN message relay systems.

A new shortwave station was brought online at Bessastadir in Northern Iceland at the beginning of the year.

Experiments with new technology in voice transmission between pilots and air traffic controllers were carried out in the autumn. The new technology, VoIP, is extensively used in public telecommunications. Its use in aircraft communications is expected to grow considerably over the next few years. In 2010, Isavia and the communication systems manufacturer, Frequentis, and PARKAIR, a manufacturer of transmitters and receivers together with Icelandair joined forces to carry out tests in which communications between pilots and air traffic controllers were carried out over VoIP exclusively. This was the first time that VoIP was tested in this manner.

VALUE

GUARANTEE

We co-operate as one toward the goal of success and excellence in service.

We respect each other's work and encourage initiative toward reformation.

GANNET LTD (FLUGFJARSKIPTI)

Isavia subsidiary Gannet ltd is responsible for communications with aircraft flying over the North Atlantic. It is an important part of Isavia's services to international aviation. The company ensures secure and efficient communications between aircraft, air traffic control centres, aircraft operators, meteorological offices and others involved in aviation. The communications centre at Gufunes is responsible for shortwave and VHF voice communications in co-operation with the telecommunications centre at Ballygireen in Ireland.

Aviation communications personnel were put under a great deal of strain during the volcanic eruption of Eyjafjallajokull. The average number of messages processed in 24 hours in 2010 was 1329. However, on the busiest days when air traffic in Icelandic was at a record high for a period of four days, an average of 4609 messages were relayed every 24 hours.

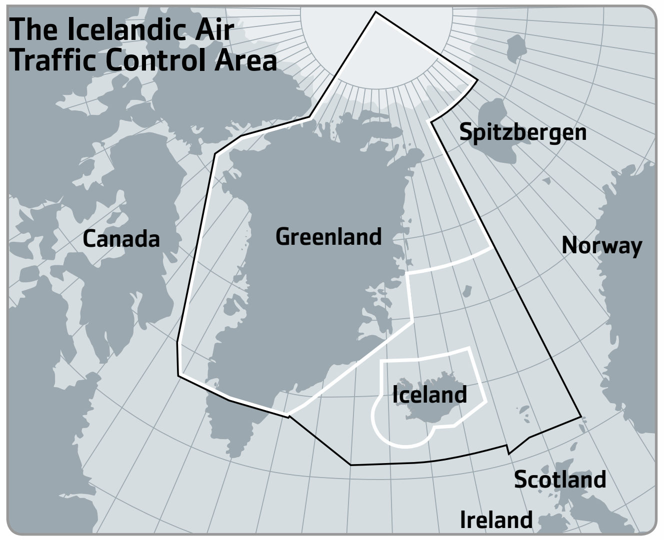
QUALITY AND SAFETY MANAGEMENT

Over the course of the year, considerable work was carried out in combining three separate quality and safety management systems into a single management system. Changes made to the operating licenses for air navigation services and flight testing required extensive co-ordination with the Icelandic Civil Aviation Authority, the Danish Civil Aviation Administration and the certification agent for the ISO 9001 standard. During the merger, over 300 documents pertaining to the Air Navigation Service Division had to be reviewed in connection with the publication of Isavia's operational manual.

EXERCISES

In 2010, an international search and rescue exercise was carried out in the Bold Mercy exercise schedule of NATO. The exercise was held before the merger and was organised by Flugstodir.

Exercises in responding to ash dispersion at jet levels have been held for many years at Iceland's instigation. These exercises were undoubtedly a great help in the preparation of the response plans that were used when real eruptions occurred in the volcanoes at Fimmvorduhals and Eyjafjallajokull in Southern Iceland. The international ash distribution exercise VOLCEX was temporarily discontinued in 2010, but two localised ash forecast and continuous training exercises, VOLCICE were held during the year.



INTERNATIONAL CO-OPERATION

Continuous efforts are made to increase efficiency in aviation. Iceland co-operates extensively with neighbouring countries in Europe. The Air Navigation Services Division in involved in numerous international programs, principally the North Atlantic Systems Planning Group (ICAO NAT SPG) where representatives of airlines, aircraft owners (IOPA) and professional organisations (IFALPA, IFATCA) resolve issues in committees and working groups.

An annual meeting is held with airlines in the North Atlantic area concerning their involvement in the International Air Navigation Service and the operating budget and investment programs for the next year.

- **INTERNATIONAL AIR NAVIGATION SERVICE**
  The International Air Navigation Service is operated on the basis of a joint finance agreement between Iceland and twenty four other countries. The International Civil Aviation Organization, ICAO, is responsible for the implementation of the agreement. Isavia is responsible for the implementation of the agreement on behalf of the Ministry of the Interior and therefore communicates extensively with ICAO. The Icelandic Meteorological Office is involved in this work along with Isavia.

- **NAT/SPG (NORTH ATLANTIC SYSTEMS PLANNING GROUP)**
  NAT/SPG is a multinational forum of the countries around the North Atlantic, and ICAO concerning the arrangement and use of the air navigation system in the North Atlantic. NAT/SPG is responsible for monitoring the overall performance of the system and encourages improvements and changes to maintain aviation safety in the area. The Director of the Air Navigation Services Division has been the chairman of NAT/SPG since 1997.

- **TRASAS/CPWG**
  Isavia participates in two committees run by ICAO that specifically address flights between North America and Asia over the North Pole. One of these is the Trans-Regional Airspace and Supporting ATM Systems Steering Group (TRASAS), a policy formulation and co-ordination committee concerning the adoption of technical innovations and operating procedures.

- **CANSO**
  CANSO is the global association of air navigation service providers. The organisation, with headquarters in Amsterdam, represents these companies in the international arena, including in dealings with ICAO, and formulates policies on behalf of its clients. Isavia became a fully valid member of CANSO in 2007.

- **CROSS POLAR WORKING GROUP (CPWG)**
  CPWG is responsible for co-ordinating working methods and the adoption of changes in the north polar region. The working group consists of representatives from all the air traffic control authorities in the area as well as representatives from the airlines operating in the area. There has been a considerable increase in air traffic in the region, and the airlines predict that their greatest increase in business in the near future will be in that region.

- **CO-OPERATION WITH THE IRISH AVIATION AUTHORITY (IAA)**
  Isavia and the IAA co-operate in the operation of the telecommunications stations at Gufunes and Ballygireen. The systems in these stations are now integrated and they can thereby operate as a single station.

- **NEAP**
  Isavia is a member of NEAP, a partnership of air navigation companies in Norway, Sweden, Denmark, Finland, Estonia, Latvia, the UK, Ireland and Iceland. The association forms a framework for collaborative projects, particularly those relating to the pan-European airspace – Single European Sky.

- **NEFAB**
  NEFAB is a project run by the NEAP countries with the aim of developing a continuous air space (Functional Airspace Block – FAB) in accordance with the Single European Sky (SES) EU directives. The area covers the air control areas of all the participating nations. A special report on the progress of the project and problems relating thereto has been prepared.

- **NORACON**
  NORACON's role is to manage NEAP's participation in the SESAR research plan. The NEAP countries are all members of NORACON together with the Austrian air traffic control company Austrocontrol. NORACON is one of sixteen partners of the SESAR Joint Undertaking, a separate body established by the EU to manage the implementation of the SESAR schedule.

- **SESAR**
  SESAR is the EU's research and development schedule geared towards developing a new generation of air traffic control systems for Europe to co-ordinate air traffic control on the continent, increase capacity and ensure flight safety. Isavia began participating in the SESAR schedule in 2009 under the auspices of NORACON. Its main focus is on air traffic control over the ocean. The project is expected to last for at least six years.

IATA RECOGNITION

The International Air Transport Association (IATA) presented Isavia with the Eagle Award in 2010 for the most improved ANSP (Air Navigation Service Provider). Isavia has been working diligently toward improving its operation and the services that the company provides as well as keeping down costs. Furthermore, IATA is of the opinion that Isavia is a leader in optimising efficiency and safety on flight paths over the North Atlantic and the North Pole.

The company and its employees are delighted with this important recognition, which is based on close, professional, technical and financial co-operation with the company's customers.

AIRPORTS AND INFRASTRUCTURE

Akureyri International Airport was the centre of international flight operations during the volcanic activity in April and May 2010 with 9,639 passengers passing through. Egilsstadir International was also busy during the same time. Isavia personnel performed stellar service during one of the greatest interference in airport services in Iceland.

Winter arrived early at Akureyri international with few snowless days till the end of the year. In Mid-November, the snow depth reached a high of 62 cm. Airport personnel remained constantly busy to keep the runway clear of snow and ice for aircraft operations.

AIRPORTS AND INFRASTRUCTURE DIVISION

As previously stated, various organisational changes were made to the structure of the companies when Flugstodir and Keflavik International Airport were merged. The name of Flugstodir's Airports and Navigations Division became the Airports and Infrastructure Division at Isavia with changed responsibilities. New construction projects were transferred to the division, as regards the development of all the installations operated by the company, such as buildings, runways, aprons, electrical utilities, lighting, etc.

The Airports and Infrastructure Division is responsible for the development of installations and equipment at all Isavia operated airports that serve domestic flights. The infrastructure service provides specialised support to other operational divisions concerning facilities construction and maintenance. This includes facilities at 50 airports and landing strips in four regional areas og which 14 airports serve scheduled domestic flight operations. The airports in Reykjavik, Akureyri and Egilsstadir are also international airports. The airport system also serves ambulance flights, tourist services, private flights and training flights.

The main operating projects as regards the airports involve the maintenance and operation of airport terminals and other buildings, runways, aircraft movement areas and lighting equipment. Snow removal, fire and rescue services are an important part of the operation. The scope of the service at each airport is in accordance with stated service levels, which depend on the nature and volume of air traffic and in some cases on geographical location. Centralised support services within the Division are responsible for providing the airports with operational support and for ensuring that they are run efficiently and economically.

The Director of the Airports and Infrastructure Division Airports is Mr. Haukur Hauksson.

QUALITY AND SAFETY MANAGEMENT

The company adopted the Opscom safety management system at Reykjavik Airport to improve the operation of the division's quality and safety management program. The system maintains all registrations and tasks at the airports and assists the airport management in supervising operational improvements.

Considerable change was made in the organisation of quality and safety management with the restructure of operational divisions of the company. Work on risk assessments for the airports in Reykjavik and Akureyri was initiated during the year, and two large risk assessment projects regarding obstacles in the vicinity of airports have been initiated in co-operation with the Norwegian airport company AVINOR.

AIRFIELD SERVICES

The reorganisation of the Airfield Services Department through economisation and integration of various job positions at airports according to Nordic models continued throughout the year. The arrangement, called "Basic Airport" in the Nordic countries, has proved a success, both as regards economisation in operations and staff welfare through a greater variety of work. It is hoped that the reorganisation will be completed within three years.

Isavia (at that time Flugstodir) took over rescue and fire service at Reykjavik Airport from the Reykjavik Area Fire Brigade on 1 March 2010. The service is performed by the Keflavik Airport Fire and Rescue Service. The implementation of the rescue and fire service is scheduled for transfer to Reykjavik Airport in 2011 as a part of the reorganisation of the airfield services.

Three aircraft accident exercises were held during the year at Isafjordur, Vopnafjordur and Bildudalur. Emphasis was placed on good co-operation with local authorities, and the exercises were a successful.

Two fire trucks were purchased in 2010 in accordance with renewal plans and in co-operation with the townships of Akureyri and Vopnafjordur. Such co-operation with the local authorities leads to better utilisation of funds, and added support to nearby communities. Two new pieces of runway clearing equipment were purchased including a powerful snow removal equipment combinations for Reykjavik Airport.

Systematic standardisation of friction testing at airports throughout Iceland was continued. Two employees have received instructor certification by the manufacturer for training and maintenance of AFST equipment.

AIRPORT SECURITY

Airport security requirements increase steadily and call for a variety of equipment and facilities for scanning passengers, luggage and cargo. Several measures must be introduced on 1 January 2011, including replacing metal detectors at international airports. The division conducted five retraining courses during the year for Isavia staff, the police and Securitas employees responsible for security screening. In addition, a separate airport security course was held for personnel from the Keflavik Airport Fire and Rescue Service who work at Reykjavik Airport, and for general and critical restricted areas at the airport.

The emergency response plan for airport security at Akureyri Airport was revised and issued in June. The project ended with a training course and a large bomb threat exercise in September, with many participants from stake holder organisations, such as the National Police Commissioner, the Coast Guard, the police and fire brigade in Akureyri, the airlines and Isavia.

VOLCANIC ERUPTIONS

A Herculean task was performed in the swift transfer of international flight operations to Akureyri and Egilsstadir when the airports at Keflavik and Reykjavik closed temporarily as a result of the volcanic eruption at Eyjafjallajokull. Isavia, airline operators and handling agents and related organisations responded quickly and transferred operational equipment and manpower to maintain uninterrupted international flight operations. Numerous different entities coordinated their efforts to solve complex tasks in a very short time and with minimum disadvantage for airport customers. Thousands of passengers and cargo were processed in the most extensive operation, the like of which has never been seen at the Akureyri and Egilsstadir airports.

CONSTRUCTION PROJECTS

The construction projects of the Airports and Infrastructure Division were performed in accordance with the National Transport Policy/Aviation. However, the limited funding available in the program only allowed the most pressing projects to be undertaken. The principal projects were the completion of the extension of the runway and security zones at Akureyri Airport and the installation of approach and lighting equipment. A 900-m-long row of approach lights was installed at Egilsstadir Airport, which now has all the required equipment for precision instrument approach procedures according to the ICAO/Cat I Standard. The equipment storage at the Vestman Islands Airport was enlarged and a new asphalt top layer was laid on one runway.

AIRPORT USER CONSULTATIONS

Good relations were maintained with the users of the airport systems through information meetings and presentations of changes to services as appropriate.

Meetings were held with aircraft operators on issues relating to construction, operations and airport security as well as co-ordination meetings with airport users concerning modification of airport charges schedules.

INTERNATIONAL PROJECTS

The Director of the Division, together with the Manager of the IT Department, undertook the implementation of a project for the Danish Development Fund (DANIDA) for three airports in Mozambique of a size that can service Boeing 737 or similar aircraft. The project involved auditing the performance of work on facilities, such as buildings, runways, aircraft movement areas, lighting and air navigation equipment and fire fighting equipment. The division took part in a co-operative project of operators of medium size airports in the Nordic countries. The project, named Benchmarking, involved the analysis and comparison of operating factors, such as the scope and cost of services to airlines and passengers at selected airports of a similar size in each country. Egilsstadir Airport was Iceland's candidate.

KEFLAVIK INTERNATIONAL AIRPORT

Keflavik International Airport is the principal airport in Iceland and a centre of international airline operations. The Eyjafjallajokull volcanic eruption prevented operations at the airport for 10 days. Despite this disruption, the total number of passengers went up by 8 per cent in 2010.

KEFLAVIK INTERNATIONAL AIRPORT

Keflavik International Airport is the principal airport in Iceland and a centre of international airline operations serving all aircraft types with a total of 22,000 general and commercial aviation flights annually and 97 per cent of the total international airline passengers in Iceland. The airport and vicinity is a hub of activity and one of the largest workplaces in the country. Mr. Eirikur Omar Sveinsson is Director, Keflavik International Airport.

AIRFIELD SERVICES

The Airfield Services Department is responsible for the operation of the airport. The operation involves the supervision and maintenance of aircraft operating areas and the clearing of obstructions and debris, supervision and maintenance of the visual navigation equipment and oil separators, bird and animal control, operation of jet aircraft arresting gears, apron management and SLOT allocation together with the operation of a maintenance shop for all of Isavia's motorised equipment at Keflavik.

Snow and ice removal is the largest task during winter months and the operation was quite successful during the year. Two new first-rate ice and snow removal equipment combinations were commissioned to replace old and obsolete equipment dating from the time of the Iceland Defence Force. There are now four new combinations in use capable of simultaneous clearing of snow from an area that previously took five of the old machines to clear. This considerably strengthens the airport equipment available to ensure safe landing conditions in the harsh winter weather at Keflavik International Airport.

FIRE AND RESCUE SERVICES

Some changes were made to the fire and rescue services during the year. The decision was made that Keflavik Airport personnel would assume responsibility for fire and rescue services at Reykjavik Airport as this was seen to lead to greater synergy and streamlining in operations. One airfield fire truck from Keflavik was loaned to Reykjavik Airport and the change was a successful.

A survey of the composition of aircraft types using the airport on a regular basis led to the decision to amend the fire response level from the CAT-9 to CAT-7 category according to ICAO's definition in consultation with the Icelandic Civil Aviation Authority. The airport's response services are able, as before, to handle the largest aircraft both as regards manpower and equipment.

CONSTRUCTION PROJECTS

Three large projects were undertaken at the Airport during the year. A top layer of asphalt was laid on 26,000 square metre area of the Haaleiti apron, and a Rhinophalt asphalt preservative was applied to 120,000 square m of aircraft taxiways. Isavia personnel conducted the Rhinophalt application as well as repairs of drain conduits at Hangar 885 on the Haaleiti apron that had been damaged by frost. The repair was within 10 per cent of the originally projected cost of renewing all the drains. Isavia personnel also erected a shelter for a ready fire truck at the runways and installed training equipment for fire fighting. Both of these projects turned out to be considerably cheaper than originally projected.

AIR TRAFFIC AT KEFLAVIK INTERNATIONAL

The total traffic of aircraft through Keflavik Airport was 52,417 movements (departures and arrivals). Thereof, 21,942 paying aircraft movements were scheduled, civil or military flights, a 3 per cent increase from the year before. Non-paying aircraft movements, such as training flights and other private flights together with flights relating to NATO air policing missions, were 30,475, an increase of 30 per cent between years.

Only seven aircraft needed to abort landing at Keflavik Airport in 2010 an only due to excessive winds or poor visibility. However, there were 26 cases where the airport was used by overflying aircraft due to unexpected events such as passenger illness or technical problems. The aircraft landed without mishap in all cases.

Fighter jets on air policing missions were stationed at the airport on three occasions during the period between March and September. A Boeing Company team with the new a B-787 "Dreamliner" aircraft conducted flight testing at the airport for a few weeks, as did a new Russian passenger plane for the same purpose. Keflavik International remains popular for flight testing of new types of aircraft, especially for crosswind tests.

Demand for fixed handling slots at the Leif Eiriksson Air Terminal for the summer schedule increased by 4.74 per cent between years. Over the winter period, the number was similar to the year before, or just under 6,000 handling slots.

VALUE

SERVICE

We minimise risk by employing disciplined operating procedures, relentless pursuit of knowledge and systematic supervision and effect safety for our customers, personnel and the public.

THE LEIF EIRIKSON AIR TERMINAL

Business was slow at the terminal during the transfer of international flight operations to Akureyri and Egilsstadir following the volcanic eruption. Terminal personnel remained busy, however, solving numerous problems related to the disruption as well as preparing for resumed operations at Keflavik.

The Eyjafjallajokull eruption had great impact on the anticipated number of passengers, but despite bleak prospects, the total number of passengers increased by eight per cent in 2010.

THE LEIF EIRIKSON AIR TERMINAL

On the merger of Keflavik International Airport and Flugstodir into Isavia, the Leif Eiriksson Air Terminal (FLE) became an operations division within the company with three operating units: the FLE Operations Department, the Keflavik Airport Security Department and the Keflavik Airport Marketing Department. The Keflavik Airport Business Division was transferred to Isavia's Finance and Administrative Division. Systematic efforts were spent on merging these two divisions in 2010. Mr Hlynur Sigurdsson is the Director of the Leif Eiriksson Air Terminal.

OPERATIONS DEPARTMENT

The FLE Operations Department is responsible for the operation and maintenance of the terminal building together with the maintenance of other property owned by the company at Keflavik International Airport. The Operations Department also provides service to retail and service outlets in the terminal building. Investment cost in 2010 amounted to 114 million Ikr for the renovation of Customs facilities in the arrival hall and upgrades to the gate control equipment in the airport parking areas.

AIRPORT SECURITY

Airport security at Keflavik International Airport conforms to the Act on Aviation and international agreements on procedures to prevent illegal actions against general aviation, passengers, employees and facilities. The operations incorporate control, implementation and supervision of airport security in collaboration with the police, customs, airport users and the Icelandic Civil Aviation Authority. The Airport Security division also performs additional duties, such as SLOT co-ordination and safety in aircraft operating areas, terminal security and the operation of the airport control centre in co-operation with Terminal operations and Airport operations. Airport security training and the issuing of restricted area access permits is also a quite extensive operation with at least 1,500 people employed by numerous organisations at the airport on the average plus summer hires.

Pressure on the Airport Aviation Security Department increased substantially as a result of the increase in passenger numbers during the year, particularly due to the 40 per cent increase in transit passengers that need to go through security scan upon arrival from America. In June, the measure was taken to

separate passengers arriving in Iceland from America from transit passengers by taking them by bus directly from the south terminal building to the arrivals hall in the north building. This measure helped to alleviate the pressure on security scanning stations in the south building, and the arrival passengers are extremely pleased with this service.

MARKETING DEPARTMENT

The Marketing Department is responsible for the internal and external marketing of Keflavik International Airport. Internal marketing involves leading the marketing committee of FLE operators to increase retail turnover, while external marketing is based on the presentation of the airport in co-operation with Isavia's Business Development Division.

Keflavik International has been elected one of the best airports in Europe for the past several years in passenger quality surveys. It was elected the best overall airport in Europe in the annual Airports Council International quality and service survey in 2009 and took second place with even higher overall score in 2010.

The Marketing Department conducted an extensive promotional campaign in Iceland and abroad that among other things resulted in greatly increased visits to the website of the airport. Visits to the Icelandic site increased by 154 per cent, from 460 thousand in 2009 to 1,168 thousand in 2010. The increase on the English language site went up by close to 330 per cent, from 161 thousand in 2009 to 688 thousand in 2010. A total of 10 airlines conducted scheduled flight operations at the airport in 2010 and the number is expected to climb to 14 in the summer of 2011.

PASSENGER VOLUME

At the beginning of the year, the number of airline passengers was expected to decrease by approximately 5 per cent in 2010 and the operating budget, therefore, was characterised by restraint and cost cutting in investments and larger maintenance projects. The volcanic eruption had extensive effects on traffic through Keflavik and the projected passenger numbers. After the eruption ended, passenger numbers improved, and there was in fact an 8 per cent increase during the year. The increase between years was greatest in transit passengers, approximately 40 per cent, while the number of arriving and departing passengers did not change. As a result, income from retail operations in the airport terminal was much better than anticipated. Despite improved operations in most outlets between years, the operating environment remains difficult. In mid-2010, a new company took over the operation of the Saga Shop and has made an effort to increase the range of Icelandic fashion items in the shop.

THE DUTY FREE STORE LTD

The Duty Free Store operates six retail shops in the Leif Eiriksson Air Terminal: a departures shop, an arrivals shop and two smaller shops in the south building. In mid-2010, the Duty Free Store took over the operation of the Saga Shop from Icelandair and made an effort to increase the range of Icelandic fashion items in the shop. The main product lines in the Duty Free Store are alcohol, tobacco, cosmetics, confectionary and now clothing, shoes and accessories.

In addition to difficult economic circumstances, it is safe to say that the eruption of Eyjafjallajokull had quite an impact on the operation of the Duty Free Store in 2010. The company's estimated loss of income was approximately ISK 12–14m per day while Keflavik Airport was closed, and it was therefore clear that the company's operation in 2010 would be more difficult than projected. The number of passengers in April decreased by 22 per cent in comparison to 2009, being 118,182 in 2009 and 91,833 in 2010. As the year progressed however, there was a considerable increase that combined with a sales campaign during the final months of the year led to better operating results by year-end than anyone dared to hope taking into account the disasters earlier in the year.

Changes were made to the company's Board in the autumn of 2010 when Mr Bergur Sigurdsson took over from Ms Drifa Snaedal. There were also changes in management. Mr Hlynur Sigurdsson joined Isavia and Ms Asta Dis Oladottir replaced him as Managing Director in September 2010, the first woman to hold the position of Managing Director in the company.

OPERATIONS AND PERFORMANCE

The company's operating revenue was approximately ISK 5,261m in 2010. Thereof, other revenues were just under ISK 40m. This is a considerable increase compared with the previous year when operating revenues were ISK 4,671m.

Operating expenses excluding cost of goods sold amounted to approximately ISK 2,671m. Thereof, rental expenses paid to the parent company were approximately ISK 1,905m. Payroll costs were approximately ISK 619m, and FTE positions increased from 92 to 99 between years. Profits before depreciation, interest and taxes (EBITDA) amounted to ISK 152m in 2010 as compared to ISK 11.7m the year before. This can be attributed first and foremost to increased sales as indicated earlier.

Company profits, after depreciation and financial items, amounted to ISK 68.2m as compared to losses of ISK 70m the year before. Net cash at year-end was approximately ISK 64m, and the company's net assets amounted to around ISK 1,198m. Liabilities amounted to ISK 663m, and equity at year-end amounted to ISK 534.8m The company equity ratio stood at 44.62 per cent at year-end.

PRINCIPAL PROJECTS

The Duty Free Store took over the operation of Saga Shop from Icelandair in July. The name of the shop was changed to Dutyfree Fashion with emphasis on a changed range of sales items. The goal is to attract a larger number of Icelandic designers and to broaden the product range.

Improvements were made to one of the Schengen shops of the Duty Free Store in the south building, and the name was changed to Iceland Dutyfree. Sales improved considerably after the changes, and it is safe to say that turnover doubled when compared to the previous year. Improvements to both the shops are expected to be completed in 2011. The alterations are geared toward ensuring that foreigners experience the shops as unique with a range of items that they don't find at other airports.

INNOVATIONS

The Duty Free Store unveiled the secret of the year and presented cosmetics from Victoria's Secret in the USA. The new items were an immediate success with the customers. In Iceland, the Victoria's Secret selection is only available in the Duty Free Store which conforms to the company's new policy of offering a unique range of products.

TERN SYSTEMS

Tern Systems hf. is a software company that, in co-operation with Isavia, has constructed most of the software systems used by the air traffic control centre in Reykjavik. Tern's role has first and foremost been to work on the development of systems tailored to Isavia's needs and to fulfil all the special needs and safety requirements of the operation, with economic considerations in mind.

The company's policy is to utilise the knowledge and experience created while working on projects for Isavia to develop its own products for international marketing. This policy has already led to several overseas projects in recent years. Tern plans to increase the proportion of its overseas operation through the sale of products, participation in software and research projects as well as services and software leasing.

Recently, increased focus has been directed at nearby markets such as the Nordic countries and other countries in Europe. Various opportunities are coming to light in Northern Europe that the company will focus on in the future, and every effort will be made to sell more in co-operation with other companies in the market.

PRINCIPAL PROJECTS

The main projects in 2010 were a flight control system in Isavia´s air traffic control centre, a training simulator in Morocco and the installation of new radar and flight data systems at Keflavik International Airport.

Tern Systems, in co-operation with Isavia, worked on the design and production of a new flight control system that supports the latest positioning technology, ADS-B. This technology will improve the ability of air traffic controllers to monitor air traffic in areas outside the range of traditional radar systems. The system, therefore, will substantially extend the areas in which Tern customers can monitor air traffic.

An agreement was made with the state-owned company ONDA in Morocco, which operates all airports and air traffic services in the country, for the delivery of a training simulator for air traffic controllers. The system is fairly large, consisting of four individual training simulators that display the conditions at the largest airports in Morocco. The installation of the system will be completed in mid-year 2011.

Another large system to be delivered by Tern in 2011 is a new air traffic control system named TAS for Keflavik Airport which is based on a system constructed in co-operation with KAC in Korea in 2007.

Tern has also strengthened its research department considerably during the year and linked it directly to Isavia's software department to meet the increase in research requirements in the company's field of operations. The research department was involved in projects in connection with the implementation of ADS-B, radar tracking and the AIRE project.

OPERATIONS AND PERFORMANCE

The company's total income amounted to ISK 338m in 2010, 19 per cent of which was income from overseas. Operating losses before depreciation and interest were approximately ISK 900 thousand while the company's overall results were negative by ISK 3.5m.

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors and shareholders of Isavia ohf.

We have audited the accompanying Consolidated Financial Statements of Isavia ohf., which comprise Statement of Financial Position as at 31 December 2010, Statement of Comprehensive Income, Statement of Changes in Equity and Statement of Cash Flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements
Management is responsible for the preparation and fair presentation of these Financial Statements in accordance with generally accepted accounting principles in Iceland. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility
Our responsibility is to express an opinion on these Financial Statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the Financial Statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the Financial Statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the Financial Statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the Financial Statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the Financial Statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the Consolidated Financial Statements give a true and fair view of the financial position of Isavia ohf. as of 31 December 2010, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as approved by the European Union.

Kópavogur, 1 April 2010

Deloitte hf.

Anna Birgitta Geirfinnsdóttir
State Authorized Public Accountant

Guðmundur Kjartansson
State Authorized Public Accountant

STATEMENT BY THE BOARD OF DIRECTORS AND CEO

Isavia ohf was established in 31 January 2010 and is a government owned public limited company and complies with the Icelandic limited companies law no. 2/1995. The company domicile and venue is located at Reykjavik Airport. The company was formed when two companies Keflavikurflugvöllur ohf. and Flugstoðir ohf. were merged together, the merger is based on law no. 153/2009. The merger between the two companies was finalized at 31 January 2010, and is effictive from 1 January 2010. Flugfjarskipti ehf., Isavia´s ohf. subsidiary merged with the company at 1 July 2010.

The Consolidated Financial Statements for the year 2010 is prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union. Keflavikurflugvöllur ohf. has in the past presented its Financial Statement in accordance to IFRS but Flugstoðir ohf. did not. The impact on the implementation of IFRS for Flugstoðir ohf. has been accounted for in the Financial Statements.

According to the Consolidated Statements of Comprehensive Income, the operating revenues of the Company amounted to ISK 14.136 million. Total comprehensive income for the year amounted to ISK 2.125 million. According to the Consolidated Statements of Financial Position, assets amount to ISK 32.069 million, the year's end book value of equity is ISK 10.302 million and the Company's equity ratio is 32%.

At year-end, there was one shareholder in the Company, the Treasury of Iceland which is the same as when the Company was established.

It is the opinion of the Board of Directors and the CEO of Isavia ohf. that the accounting policies used are appropriate and that these Consolidated Financial Statements present all the information necessary to give a true and fair view of the company's assets and liabilities, financial position and operating performance, as well as describing the principal risk and uncertainty factors faced by the Company.

The Board of Directors and the CEO hereby confirm the Consolidated Financial Statements for the year 2010.

Vestmannaeyjar, 1 April 2011

Board of Directors

Þórólfur Árnason
Chairman of the Board

Rannveig Guðmundsdóttir

Arnbjörg Sveinsdóttir

Arngrímur Jóhannsson

Ásta Rut Jónasdóttir

Jón Norðfjörð

Ragnar Óskarsson

CEO

Björn Óli Hauksson

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME 2010

	Notes	Consolidation 2010
Operating revenues	5	14.135.853.449
Cost of goods sold		(2.502.617.146)
Salaries and related expenses	6	(6.193.813.269)
Administrative expenses		(617.712.535)
Other operating expenses		(1.777.083.000)
Depreciation and amortization	9, 10	(1.321.226.252)
Operating profit		1.723.401.247
Non-controlling interest		795.942
Financial income	7	218.640.386
Financial expenses	7	(774.023.211)
Net gain arising on financial assets and liabilities	7	1.398.578.668
Profit before taxes		2.567.393.032
Income tax	8	(442.216.088)
Total comprehensive income for the year		2.125.176.944

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

Assets	Notes	Consolidation 31.12.2010	01.01.2010
Non-current assets			
Property, plant and equipment	9	22.016.631.821	22.382.146.119
Intangible assets	10	6.224.146.206	6.395.358.500
Bonds and other long term assets	12	182.741.353	242.671.577
Deferred tax assets	19	236.848.317	652.099.273
		28.660.367.697	29.672.275.469
Current assets			
Inventories	13	369.920.223	321.838.801
Accounts receivables	14	1.063.860.059	904.037.782
Current maturities of long term assets	12	89.634.609	69.441.622
Other receivables	14	378.975.750	145.193.771
Bank balances and cash	14	1.506.340.263	1.895.465.133
		3.408.730.904	3.335.977.109
Total assets		32.069.098.601	33.008.252.578
Equity and liabilities			
Equity	15		
Share capital		5.589.063.362	5.589.063.362
Statutory reserves		2.483.798.000	2.483.798.000
Revaluation reserves		55.156.060	0
Retained earnings		2.175.359.409	50.182.465
Equity attributable to owners of the company		10.303.376.831	8.123.043.827
Non-controlling interest		(1.143.819)	(347.877)
Total equity		10.302.233.012	8.122.695.950
Non-current liabilities			
Loans from credit institutions	16	18.342.130.504	20.867.111.650
Obligations under finance leases	17	5.579.247	16.219.553
Deferred tax liabilities	19	32.875.072	13.889.631
		18.380.584.823	20.897.220.834
Current liabilities			
Accounts payable	20	530.873.228	988.092.373
Government treasury		389.971.326	547.821.377
Current maturities of non-current liabilities	20	1.356.803.204	1.325.280.293
Current tax liabilities	8	20.087.121	57.006.443
Other current liabilities	20	1.088.545.887	1.070.135.307
		3.386.280.766	3.988.335.793
Liabilities		21.766.865.589	24.885.556.628
Total equity and liabilities		32.069.098.601	33.008.252.578

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

	Share Capital	Statutory reserves	Revaluation reserves	Retained earnings	Total Equity
Opening balance from Treasury	10.000.000	0	0	0	10.000.000
Opening balance from Flugstoðir ohf.	1.579.063.362	101.500.000	0	756.325.332	2.436.888.694
Opening balance from Keflavíkurflugvöllur ohf.	4.000.000.000	2.382.298.000	0	(448.059.985)	5.934.238.015
Changes in deferred tax assets 1.1.2010	0	0	0	(11.686.352)	(11.686.352)
Impact of IFRS	0	0	0	(246.396.530)	(246.396.530)
Opening balance at 1 January 2010	5.589.063.362	2.483.798.000	0	50.182.465	8.123.043.827
Revaluation of subsidiaries assets	0	0	55.156.060	0	55.156.060
Comprehensive income for 2010	0	0	0	2.125.176.944	2.125.176.944
Equity attributable to owners of the company	5.589.063.362	2.483.798.000	55.156.060	2.175.359.409	10.303.376.831
Non-controlling interest in equity	0	0	0	0	(1.143.819)
Balance at 31 December 2010	5.589.063.362	2.483.798.000	55.156.060	2.175.359.409	10.302.233.012

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Notes	Consolidation 2010
Cash flows from operating activities		
Operating profit		1.723.401.247
Depreciation and amortization	9, 10	1.321.226.252
Long term assets expensed	12	57.924.552
Gain on disposal of assets		(13.620.562)
Operating cash flow before movement in working capital		3.088.931.489
Increase in inventories		(48.081.422)
Increase in operating assets		(375.624.598)
Decrease in operating liabilities		(548.792.722)
Cash generated from operations		2.116.432.747
Interest earned		349.144.529
Finance costs		(818.482.496)
Income taxes paid		(57.006.442)
Net cash generated from operating activities		1.590.088.338
Investing activities		
Purchases/sales of property, plant and equipment	9	(646.054.514)
Purchases of intangible assets	10	(57.561.094)
Purchases of bonds		(36.518.016)
Installments on bonds		25.407.956
		(714.725.668)
Financing activities		
Repayments of borrowings		(1.237.233.794)
Repayments of obligations under finance leases		(9.449.495)
		(1.246.683.289)
Net decrease in cash and cash equivalents		(371.320.619)
Cash and cash equivalants at the beginning of the year		1.895.465.133
Effect of foreign exchange rates		(17.804.251)
Cash and cash equivalants at the end of the year		1.506.340.263
Other items:		
Working capital from operations	26	2.562.587.080

1. General information

Isavia ohf. (the Company) was established at 31 January 2010 and is a government owned public limited company and complies with the Icelandic limited companies law no. 2/1995. The company domicile and venue is located at Reykjavik Airport.

At 29 December 2009 new law no. 153/2009 was implemented on merger between the two public limited companies, Flugstoðir ohf. and Keflavíkurflugvöllur ohf. A new public limited company was to be established and according to paragraph 5 of law no. 153/2009 the newly established company shall take over all rights and obligations of the two public companies mentioned in law no. 102/2006 and law no. 76/2008. The takeover does not give the negotiating parties, which the merger may concern, permission to terminate existing contract relationships.

Isavia ohf. and Flugfjarskipti ehf. merged on 1 July 2010. Flugfjarskipti ehf. specialised in air navigation in fields of telecommunications in connection with North-Atlantic ocean flights. Flugfjarskipti ehf. was wholly owned subsidiary of Isavia ohf. and no new shares were issued due to the merger.

The Consolidated Financial Statements of Isavia ohf. consist of the parent and its subsidiaries. Companies within the consolidation are in addition to Isavia ohf., Fríhöfnin ehf. and TERN SYSTEMS hf.

2. Application of new and revised International Financial Reporting Standards (IFRSs)

The Consolidated Financial Statement have been prepared in accordance with international financial reporting standards (IFRSs), as they are adopted by the European Union at the end of 2010, changes to them and new interpretations. It is the boards opinion that an implementation of new and revised IFRSs has no material effect on the Financial Statement. The Company has not applied new and revised IFRSs which have been published but not yet effective.

3. Summary of Significant Accounting Policies

Statement of compliance

Isavia ohf. now present their first Financial Statement in accordance with International Financial Accounting Standards, IFRS as adopted by the European Union. The transition to IFRS was done in compliance with IFRS 1 instructions on implimentation of International Financial Accounting Standards. The transition was made at 1 January 2010.

Basis of preparation

The Consolidated Financial Statements have been prepared on the historical cost basis. The Financial Statements are presented in ISK, which is the Company's functional currency.

To provide more information the opening balance at 1 January 2010 is presented in the Statement of Financial Position in addition to the ending balance at the end of year 2010.

The principal accounting policies are set out below.

Estimates and decisions

At the making of the Consolidated Financial Statements, the Management, in accordance with International Financial Reporting Standards, need to make decisions, estimate and draw conclusions which affect assets and liabilities at the reporting date, information in the notes and income and cost. All conclusions and estimates are based on knowledge and experience and other relevant factors and make up the basis for decisions made on book value of assets and liabilities which can not be ascertained by any other mean.

All changes in accounting estimates are recognised in the period they incur.

NOTES

3. Summary of Significant Accounting Policies (continued)

Basis of consolidation

The Consolidated Financial Statements incorporate the Financial Statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an investee enterprise so as to obtain benefits from its activities.

The Consolidated Financial Statements have been prepared using the purchase method. When ownership in subsidiaries is less than 100%, the non-controlling interest in the subsidiaries' profit or loss and stockholders equity at end of period are identified separately. Immaterial minority interest is not identified in the Consolidated Financial Statements.

The result of subsidiaries acquired during the year are included in the Consolidated Income Statement from the effective date of acquisition as appropriate. Where necessary, adjustments are made to the Financial Statements of subsidiaries to bring their accounting policies into line with those used by other members of the Company.

One of the purposes of consolidated financial statements is to show only the net external sales, expenses, assets and liabilities of the consolidated entities as a whole. Hence, intercompany transactions have been eliminated within the consolidated businesses in the presentation of the consolidated financial statements.

Risk management

The Company's Board of Directors has an overall plan towards risk management. The Company has no interest rate or currency swap contracts outstanding at year end.

Revenue recognition

Revenues are recognised when earned as required by International Financial Reporting Standards.

Interest income is accrued over time, by reference to the principal outstanding and at the interest rate appliceble.

Construction contracts

Where the outcome of a construction contract can be estimated reliably, revenue and costs are recognised by reference to the stage of completion of the contract activity at the balance sheet date, measured based on the proportion of contract costs incurred for work performed to date relative to the estimated total contract costs, except where this would not be representative of the stage of completion. Variations in contract work, claims and incentive payments are included to the extent that they have been agreed upon.

Where the outcome of a construction contract cannot be estimated reliably, contract revenue is recognised to the extent of contract costs incurred that is probable to be recoverable. Contract costs are recognised as expenses in the period in which they incur.

When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases. Assets held under finance leases are recognised as assets of the Company at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor

3. Summary of Significant Accounting Policies (continued)

Foreign currencies

The Company's Financial Statement are prepared in the currency most of the underlying transaction and operations in which it primarily generates and expends cash, the functional currency.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

Income tax

Income tax is calculated and recognised in the Financial Statements. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other periods and it further excludes items that are never taxable or deductible.

The tax currently payable is income tax that is likely to be paid within the next 12 months for taxable income of the year and corrections in income tax for pervious years.

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the Financial Statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. The difference is due to different assumptions in calculation of income tax.

Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilized.

Property, plant and equipment

Property, plant and equipment are recognised as an asset when it is probable that future economic benefits associated with the asset will flow to the Company and the cost of the asset can be measured in a reliable manner.

Buildings and sites are revalued at the end of the reporting period and the revaluation is recognised in revaluation reserves in equity. The revaluation reflects the fair value of the asset on the reporting date less any accumulated depreciation and impairment losses. On a regular basis an assasment should be made if there is a considerable difference between the revalued carrying amount and the fair value of the asset. If the fair value is lower than previously assessed revaluation it is charged to the income statement. Depreciation of revalued buildings and site are charged to the income statement.

The cost of a property, plant and equipment comprises its purchase price and any directly attributable cost of bringing the asset to working condition for its intended use.

The depreciable amount of the asset is allocated on a straight-line basis over its useful life, less residual value. The depreciation charge for each period is recognised as an expense. The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

Assets held under finance lease are depreciated over their expected useful lives on the same basis as owned assets.

3. Summary of Significant Accounting Policies (continued)

Intangible assets

Intangible assets are recognised only if it is probable that the asset will generate future economic benefits and the cost of the asset can be measured reliably. Intangible assets include business agreements, trademarks ans softwares. Intangible asset which qualifies for recognition as an asset is initially measured at cost. The depreciable amount of the asset is allocated on a fixed annual percentage of the historical cost over its useful life, less residual value.

Intangible assets resulting from the merger of the companies are only accounted for if they are distinctive from goodwill. At the initial registration they are recognized at cost, but with later assesments they are stated at cost less accumulated depreciations and impairment losses.

Impairment

At the end of each reporting period, the Company reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any).

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or a cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (or cash-generating unit) in prior years.

Inventories

Inventories are stated at the lower of cost or net realisable value, after taking obsolete and defective goods into consideration. Net realisable value represents the estimated selling price less all estimated costs to completion and costs to be incurred in marketing, selling and distribution.

Bonds and long-term receivables

Bonds and long-term receivables which the Company has the expressed intention and ability to hold to maturity (Loans and receivables) are valued at cost, less an allowance for estimated irrecoverable amounts.

Accounts receivables

Accounts receivables are valued at nominal value less an allowance for doubtful accounts. The allowance is deducted from accounts receivable in the balance sheet and does not represent a final write-off.

Long term liabilities

Loans from credit institutions and other non-current liabilities are valued at nominal value less payments made and the remaining nominal balance is adjusted by exchange rate or index, if applicable. Interest expense is accrued on a periodical basis, based on the principal outstanding and at the interest rate applicable. Borrowing costs are recognised in profit or loss in the year they are incurred.

3. Summary of Significant Accounting Policies (continued)

Accounts payable

Accounts payable are valued at nominal value and accounts payable in other currencies have been booked at the exchange rates prevailing on the balance sheet date.

Provisions

Provisions are recognised when the Company has a present obligation as a result of a past event, and it is probable that the Company will be required to settle that obligation.

Provisions for product liabilites are booked at the date of sale on the relevant goods and revalued by management in accordance to expected payout which the provisions could entail.

Financial assets

Financial assets are classified into the following specified categories: financial assets 'at fair value through profit or loss' (FVTPL), 'held-to-maturity' investments, 'available-for-sale' (AFS) financial assets and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.
All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a debt instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

Income is recognised on an effective interest basis for debt instruments other than those financial assets classified as at FVTPL.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are measured at amortised cost using the effective interest method, less any impairment.
Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

Impairment of financial assets

Financial assets, other than those at FVTPL, are assessed for impairment at the end of each reporting period to evaluate if there has been an impairment to the asset. Financial assets are considered to be impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial assets, the estimated future cash flows of the asset has been affected. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the cost would have been had the impairment not been recognised.

3. Summary of Significant Accounting Policies (continued)

Financial liabilities and equity instruments

Classification as debt or equity

Debt and equity instruments issued by the Company are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument.

Financial liabilities

Financial liabilities are classified as either financial liabilities 'at FVTPL' or 'other financial liabilities'.

Financial liabilities at FVTPL

Financial liabilities are classified as at FVTPL when the financial liability is either held for trading or it is designated as at FVTPL.

A financial liability other than a financial liability held for trading may be designated as at FVTPL upon initial recognition if:

- Such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- The financial liability forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Company's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 Financial Instruments: Recognition and Measurement permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Other financial liabilities

Other financial liabilities (including borrowings) are subsequently measured at amortised cost using the effective interest method.

4. Critical accounting judgements and key sources of estimation uncertainty

In the application of the Company's accounting policies, which are described in note 3, the directors are required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

5. Revenues

The consolidated composition of revenues, is specified as follows	2010
Revenue from sales	5.232.332.361
Revenue from services	7.273.230.677
Revenue from long term assets	1.630.290.411
	14.135.853.449

6. Salaries and related expenses

	2010
Salaries	4.733.899.003
Pension fund	633.069.648
Payroll taxes	463.991.650
Salary-related expenses	82.885.417
Pension and vaction pay obligation	159.689.208
Capitalized employment expenses	(29.399.236)
Other employee expenses	149.677.579
	6.193.813.269
Average number of employees	707

The Company´s total management salaries and benefits for the year 2010 was 71,3 million ISK.

7. Financial income and expenses

Financial income

	2010
Interest on bank deposits	69.721.247
Interest revenue from bonds and other long term assets	114.353.268
Other interest revenue	34.565.871
	218.640.386

Financial expenses

	2010
Interest expense and indexation	(767.212.914)
Bank costs	(2.550.538)
Interest on late payments	(4.259.759)
	(774.023.211)

Net gain (loss) from financial assets and liabilities

	2010
Net exchange rate differences	1.398.578.668
	1.398.578.668

8. Income tax

Income tax has been calculated and recorded in the Financial Statements, the amount charged in the Income Statement is ISK 442,2 million. Income tax payable in the year 2011 is ISK 20,1 million.

The effective tax rate is specified as follows:

	2010 Amount	%
Profit before taxes	2.567.393.032	
Tax at the rate of 18%	(462.130.746)	18,0%
Change in tax rate	(20.397.328)	-0,8%
Other items	40.311.986	1,6%
Income tax according to Statement of Comprehensive Income	(442.216.088)	-17,2%

9. Property, plant and equipment

	Buildings and artwork	Loading bridges and car parks	Fixtures and machinery	Other assets	Total
Cost					
Balance at 1 January 2010	19.197.803.846	2.228.473.548	2.042.626.178	4.154.135.993	27.623.039.565
Revaluation	67.263.488	0	0	0	67.263.488
Additions	43.901.676	83.306.241	59.218.949	478.508.360	664.935.226
Disposals	0	0	0	(23.031.518)	(23.031.518)
Balance at 31 December 2010	19.308.969.010	2.311.779.789	2.101.845.127	4.609.612.835	28.332.206.761
Accumulated depreciation					
Balance at 1 January 2010	2.342.725.327	544.177.892	807.338.481	1.546.651.746	5.240.893.446
Charge for the year	465.822.335	86.620.378	146.356.088	390.702.630	1.089.501.431
Disposals	0	0	0	(14.819.937)	(14.819.937)
Balance at 31 December 2010	2.808.547.662	630.798.270	953.694.569	1.922.534.439	6.315.574.940
Book value					
Book value 1 January 2010	16.855.078.519	1.684.295.656	1.235.287.697	2.607.484.247	22.382.146.119
Book value at year end	16.500.421.348	1.680.981.519	1.148.150.558	2.687.078.396	22.016.631.821
Depreciation rates	1-14%	2-20%	5-35%	7-33%	

With the merger of Flugfjarskipti ehf. and Isavia ohf. the properties of the former company were revaluated because the market value of their properties were considered higher than the book value. The revaluation is based on an estimated sale price, which has been confirmed by appropriated assessor. The changes in the value is credited to other equity as revaluation reserve and the tax effect in deferred tax liability.

Information about the revalued properties in year end:

	31.12.2010
Revalued book value	136.080.000
Impact of the special revaluation	(67.263.488)
Book value without impact of revaluation	68.816.512

The assessment- and insurance value for the Company's assets is itemized as the following:

Consolidation	Assessment value	Insurance value
Buildings and sites	17.376.666.000	27.972.160.000
Machinery and equipment, asset insurances	0	10.492.591.615
Other insurances	0	250.000.000

The Company has pledged it´s real estates and sites for its borrowings from credit institutions. Mortgages by the Company with a remaining loan balance of ISK 15,8 billion at year-end are registered against the fixed assets of the Company of book value of ISK 16,9 billion at the same time.

10. Intangible assets

Consolidation	Usage agreement on facilities	Usage agreement on runways	Software	Total
Cost				
Balance at 1 January 2010	477.035.000	5.706.000.000	468.528.486	6.651.563.486
Additions	0	0	60.512.525	60.512.525
Balance at 31 December 2010	477.035.000	5.706.000.000	529.041.011	6.712.076.011
Amortization				
Balance at 1 January 2010	15.901.167	190.200.000	50.103.819	256.204.986
Charge for the year	15.901.167	190.200.000	25.623.654	231.724.821
Balance at 31 December 2010	31.802.334	380.400.000	75.727.472	487.929.806
Book value				
Book value 1 January 2010	461.133.833	5.515.800.000	418.424.667	6.395.358.500
Book value at year end	445.232.666	5.325.600.000	453.313.539	6.224.146.206
Depreciation rates	3,3%	3,3%	20%	

According to an agreement between Keflavíkurflugvöllur ohf. and The Icelandic Defence Agency which was signed on 22 April 2009, Keflavíkurflugvöllur ohf. took over certain NATO facilities and equipment for the next 30 years from the beginning of 2009. No fees will be charged for the usage but Keflavíkurflugvöllur ohf. is obliged to cover all costs of daily operating and maintenance expenses, to ensure that their condition is in accordance with standards put forth by The International Civil Aviation Organization. The Icelandic Defence Agency on behalf of NATO, has the right to use theses facilities. The agreement for usage is amortizied on a straight-line bases over the useful life of the agreements.

11. The Consolidation

The Consolidated Financial Statements of Isavia ohf. consists of the parent and the following subsidiary:

	Ownership%	Nominal amount	Principal activity
Shares in subsidiaries			
Fríhöfnin ehf., Keflavík Airport	100,00%	50.000.000	Retail and commerce
Tern Systems hf., Kópavogi	77,00%	36.863.636	Software and consulting
Flugfjarskipti ehf., Reykjavík 1/1-30/6	100,00%	250.500.000	Telecommunication

12. Bonds and other long term assets

Bonds

	31.12.2010	01.01.2010
Opening balance at the beginning of the year	71.969.333	168.733.635
Installments during the year	(16.987.114)	0
Additions	3.012.000	0
Additions through merger	95.277.623	0
Price indexation changes	143.092	0
Book value at year end	153.414.934	168.733.635
Current maturities	(21.169.943)	(24.032.982)
	132.244.991	144.700.653

12. Bonds and other long term assets (continued)

Long term receivable

	31.12.2010	01.01.2010
Opening balance at the beginning of the year	143.379.564	143.379.564
Additions	33.506.016	0
Charge for the year	(57.924.552)	0
Book value at year end	118.961.028	143.379.564
Current maturities	(68.464.666)	(45.408.640)
	50.496.362	97.970.924
Bonds and other long term assets at year end	182.741.353	242.671.577

13. Inventories

	31.12.2010	01.01.2010
Supply inventory	13.008.336	12.438.565
Goods for resale	358.911.943	305.453.115
Goods in transit	5.772.387	16.500.000
Allowance for old and obsolete inventory	(7.772.443)	(12.552.879)
	369.920.223	321.838.801
Insurance value of inventories	521.101.044	459.125.434

No inventories have been pledged at year end 2010.

14. Other financial assets

Accounts receivables

	31.12.2010	01.01.2010
Domestic receivables	891.900.721	773.581.993
Foreign receivables	146.695.526	156.086.935
Income not invoiced	50.357.812	0
Allowances for doubtful accounts	(25.094.000)	(25.631.146)
	1.063.860.059	904.037.782

Changes in the allowance for doubtful accounts:

	31.12.2010	01.01.2010
At the beginning of the year	(24.631.146)	(25.631.146)
Allowance for doubtful accounts	(14.291.737)	0
Impairment loss recognised on receivables	13.828.883	0
At year end	(25.094.000)	(25.631.146)

Allowance has been made for doubtful accounts, this allowance has been determined by management in reference to past default experience.

NOTES

14. Other financial assets (continued)

Other receivables

	31.12.2010	01.01.2010
Value added tax, receivables	108.255.836	87.278.776
Prepaid expenses	18.093.324	14.668.456
Capital income tax	21.882.881	26.907.375
Accrued interest, receivables	4.855.031	1.291.967
Prepaid lunch vouchers from employees	2.834.520	3.506.800
Overpaid taxes	24.110.670	0
Accrued income, receivables	48.084.556	0
Work in progress, special project due to grants	35.501.089	11.540.397
Other receivables	115.357.843	0
	378.975.750	145.193.771

Bank balances and cash

The Company´s cash and cash equivalent consist of cash and bank balances.

	31.12.2010	01.01.2010
Bank balances in ISK	1.267.982.556	1.626.913.957
Bank balances in foreign currencies	234.869.118	263.680.796
Cash in ISK	3.488.589	3.213.670
Cash in foreign currency	0	1.656.710
	1.506.340.263	1.895.465.133

15. Equity

Share capital is specified as follows:

	Shares	Ratio	Amount
Total share capital at year end	5.589.063.362	100,0%	5.589.063.362
	5.589.063.362	100,0%	5.589.063.362

Each share of one ISK carries one vote. The Ministry of Finance carries the voting rights on behalf of the Icelandic Treasury. All shares have been paid in full.

NOTES

16. Long term borrowings

Consolidation	Loans from credit institutions 31.12.2010	01.01.2010
Debts in CHF	3.969.103.290	4.063.331.313
Debts in EUR	4.040.370.428	5.153.313.321
Debts in GBP	1.710.676.569	2.008.883.278
Debts in JPY	1.372.720.652	1.363.712.444
Debts in SEK	769.146.504	816.499.222
Debts in USD	5.391.711.098	6.337.873.721
Debts in ISK	2.435.499.403	2.439.718.807
	19.689.227.944	22.183.332.106
Amount due for settlement within 12 months	(1.347.097.440)	(1.316.220.456)
Non-current liabilities at year end	18.342.130.504	20.867.111.650

Installments of non-current liabilities are specified as follows:

	Loans from credit institutions
Current maturities	1.347.097.440
Installments in 2012	1.275.754.884
Installments in 2013	1.254.011.715
Installments in 2014	1.242.663.566
Installments in 2015	1.220.055.655
Installments later	13.349.644.684
	19.689.227.944

17. Obligations under finance leases

	Lease payments not due 31.12.2010	01.01.2010	Present value of minimum lease payments 31.12.2010	01.01.2010
Amounts payable within one year	9.977.277	10.234.329	9.705.764	9.059.837
Amounts payable later	5.823.379	17.405.542	5.579.247	16.219.553
	15.800.656	27.639.871	15.285.011	25.279.390
Future finance charges	(515.645)	(2.360.481)		
Present value of lease obligation	15.285.011	25.279.390		

18. Retirement benefit obligation

Isavia ohf. and Fríhöfnin ehf. are responsible for the retirement benefit obligation arising in excess of total premium related to their employees each year. The Company is not responsible for total retirement benefit obligations for its employees that belong to the B part of The Pension Fund for State Employees but only the additional payments so the retirement benefit obligations for each employee will be met. In the year 2010 the total amount charge through profit or loss is ISK 97,8 million.

19. Deferred tax assets / (liability)

Consolidation	Defered tax assets	Deferred tax liabilities
Opening balance at 1 January 2010	652.099.273	(13.889.631)
Addition due to the merger	(12.107.430)	0
Effect of change in tax rate	23.684.832	(3.287.507)
Calculated income tax for the year 2010	(446.915.479)	(15.697.934)
Tax payable in the year 2011 due to a subsidiary	20.087.121	0
Deferred tax at year end	236.848.317	(32.875.072)

Deferred tax balances consist of the following account balances	Defered tax assets	Deferred tax liabilities
Property, plant and equipment	(1.102.971.200)	(34.264.847)
Current assets	96.279.071	0
Other items	(137.125.095)	1.389.775
Tax loss carried forward	1.380.665.541	0
	236.848.317	(32.875.072)

Tax loss carried forward can be used against taxable profit, as specified:

Available for the years 2011 through 2017	258.943.979
Available to the year 2018	7.011.293.416
Available later	34.708.830
	7.304.946.225

20. Other financial liabilities

Accounts payable

	31.12.2010	01.01.2010
Domestic accounts payable	440.142.893	926.158.647
Foreign accounts payable	90.730.335	61.933.726
	530.873.228	988.092.373

Other current liabilities

	31.12.2010	01.01.2010
Value added tax, payable	52.980.121	32.884.136
Deferred revenue	4.052.009	17.190.854
Tax payable	4.276.883	5.662.582
Work in progress	5.500.000	12.500.000
Accrued pension contribution to The Pension Fund for State Employees	73.020.385	61.668.842
Salaries and related expenses payable	236.400.412	322.477.345
Accrued holiday commitment	515.161.311	342.155.138
Accrued interest, payable	169.290.916	210.933.679
Other liabilities	27.863.850	64.662.731
	1.088.545.887	1.070.135.307

Current maturities of long-term liabilities

	31.12.2010	01.01.2010
Loans from credit institutions	1.347.097.440	1.316.220.456
Obligation under finance leases	9.705.764	9.059.837
	1.356.803.204	1.325.280.293

21. Financial risk

Financial instruments

The consolidated financial assets and liabilities are specified into following types of financial instruments:

Financial assets	31.12.2010
Bank balance and cash	1.506.340.263
Loans and receivables	1.578.157.419

Financial liabilities	31.12.2010
Other financial liabilities	21.733.990.517

Financial assets which are intended to hold to maturity, loans and advances and other financial liabilities are measured at amortized cost with effective interest method less impairment.

Risk management

The Company's management monitors and manages the financial risks relating to the operations of the Company. These risks include interest rate risk, currency risk, market risk, credit risk and liquidity risk.

Interest rate risk

Interest rate risk is the risk that fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

Interest rate changes affect the expected cash flow of assets and liabilities which bear floating interest rates. Interest rate risk is only applicable to interest bearing assets since the liabilites of the Company only bear fixed interest rates.

Sensitivity analysis

In the analysis below the effects of 50 and 100 basis points increase on profit or loss and equity are demonstrated. The sensitivity analysis below has been determined based on the exposure to interest rates at the balance sheet date. The analysis is prepared assuming the amount outstanding at the balance sheet date was outstanding for the whole year. The analysis assumes that all other variables than basis points are held constant. The sensitivity analysis does take into account tax effects. A positive amount below indicates an increase in profit and other equity. A decrease in basis points would have an opposite impact on income statement and equity.

Effects on profit or loss and other equity are the same as change in valuation of the underlying financial instruments is not charged directly to equity. Positive amount indicates increased profits and equity. Lower interest rates would have the same effect but in the opposite direction:

	31.12.2010	
	50 bps.	100 bps.
Effects on profit or loss and other equity	(66.667.779)	(133.335.558)

21. Financial risk (continued)

Foreign currency risk

Foreign currency risk is the risk that fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign currency rates.

Foreign currency risk exposure does arise when there is a difference between assets and liabilities denominated in foreign currency.

The majority of assets of the Company are in the local currency, but some of the financial assets are denominated in foreign currency. The majority of the liabilities of the Company are denominated in foreign currencies. Following table details the currencies that affect the operations of the Company. Rates and volatility in exhange rates are based on mid rates.

	Year-end rate		Average rate		Volatility
Currency	2010	2009	2010	2009	2010
EUR	153,80	179,88	161,89	172,67	4,3%
GBP	178,47	201,60	188,55	193,89	9,1%
JPY	1,41	1,35	1,39	1,33	14,2%
DKK	20,64	24,17	21,74	23,19	4,3%
NOK	19,67	21,67	20,21	19,80	8,8%
SEK	17,16	17,52	16,96	16,30	8,4%
USD	115,05	124,90	122,04	123,59	11,0%
CHF	122,91	121,26	117,24	114,32	9,4%
CAD	115,26	119,04	118,46	109,04	11,8%

Foreign currency risk 31.12.2010

	Assets	Liabilities	Net balance
EUR	80.948.592	4.087.042.466	(4.006.093.874)
GBP	38.617.929	1.719.730.847	(1.681.112.918)
JPY	769.644	1.372.720.652	(1.371.951.008)
CHF	2.152.503	3.980.946.100	(3.978.793.597)
DKK	64.044.439	3.653.528	60.390.911
NOK	4.173.559	6.962.732	(2.789.173)
SEK	2.142.204	769.146.504	(767.004.300)
USD	205.338.701	5.404.348.157	(5.199.009.456)
CAD	156.841	0	156.841

Sensitivity analysis

The table below shows what effects 5% and 10% increase of the relevant foreign currency rate against the ISK would have on profit or loss and other equity. The table above details monetary assets and liabilities that are denomintated in foreign currency and the sensitivity analysis apply to. The foreign currency assets and liabilities in the sensitivity analysis are mainly foreign currency borrowings and foreign currency bank balances. The analysis assumes that all other variables than the relevant foreign currency rate are held constant. The sensitivity analysis does take into account tax effects. A positive amounts below indicates an increase in profit and other equity. A decrease of the relevant foreign currency rate against the ISK would have an opposite impact on profit or and other equity.

Effects on profit or loss and equity	**31.12.2010**	
	5%	10%
EUR	(164.249.849)	(328.499.698)
GBP	(68.925.630)	(137.851.259)
JPY	(56.249.991)	(112.499.983)
CHF	(163.130.537)	(326.261.075)
DKK	2.476.027	4.952.055
NOK	(114.356)	(228.712)
SED	(31.447.176)	(62.894.353)
USD	(213.159.388)	(426.318.775)
CAD	6.430	12.861

21. Financial risk (continued)

Credit risk

Credit risk refers to the risk that a counterparty will default on its contractual obligations resulting in financial loss to the Company. The Company monitors the credit risk development on a regular basis.

Maximum credit risk	**Carrying amount** 31.12.2010
Bonds and other long term assets	153.414.934
Accounts receivables	1.063.860.059
Other receivables	360.882.426
Bank balances and cash	1.506.340.263
	3.084.497.682

The maximum risk of the Company is the carrying amount itemized above.

Liquidity risk management

Liquidity risk is the risk that the company has difficulties to meet its financial commitments in the near future.

On a regular basis the Company monitors the liquidity balance, development and the effects of market environment.

	Payable within 1 year	Payable between 1 - 4 years	Payable after 4 years	Total
Liabilities 31.12.2010				
Non-interest bearing	2.029.477.562	0	0	2.029.477.562
Floating interest rates	1.146.784.749	427.498.858	12.072.877.081	13.647.160.688
Fixed interest rates	225.688.025	4.570.566.209	1.261.098.034	6.057.352.268
	3.401.950.336	4.998.065.067	13.333.975.115	21.733.990.518
Assets 31.12.2010				
Non-interest bearing	1.433.223.657	35.789.488	52.871.758	1.521.884.903
Floating interest rates	1.516.245.667	39.621.616	3.962.130	1.559.829.413
Fixed interest rates	2.783.366	0	0	2.783.366
	2.952.252.690	75.411.104	56.833.888	3.084.497.682
Net balance 31.12.2010	(363.139.655)	(4.872.157.601)	(13.277.141.227)	(18.512.438.483)

22. Other issues

Revenues of International flight service

On the basis of the service agreement with the Ministry of Interior, the Company offers an air navigation services within the Icelandic airspace and a part of the flight territory for Greenland and the Faroe Island in accordance with the Icelandic Treasury´s commitments in international agreements. For this obligation there is a so called Joint Financing Agreement which was signed in the year 1956 between 13 member countries of ICAO but these members has since reached 24 in total. The users of the service pays for the service in full.

23. Other obligations

Operating licence

Isavia ohf. has received a licence from the Iceland Civil Aviation Administration for five years for the opertion of airports and air navigation services according to regulation no. 631/2008. Keflavíkurflugvöllur has received an airport certification for five years as well as certification according the regulations on airports in Iceland.

Under its operating licence the Company shall be obliged to respect and meet all obligations within the range of responsibilities and the operational area of the airport, the runways and terminals itself at Keflavíkurflugvöllur which the Icelandic goverment has undertaken, and may undertake.

In times of war, and in emergencies, the Company shall be obliged to grant the American Military Authorities in accordance with the U.S - Iceland defence agreement, the use of the airports facilities. The Defense Department of the Ministry for Foreign Affairs shall be responsible for all liaising between the Company and the American Military Authorities, whether directly or indirectly.

Service aggreement for construction

The service aggreement between the Ministry of the Interior and the company (formerly Flugstoðir) applies to maintainance and construction of airports. The company works with the Ministry of the Interior and puts forth a proposals for maintance and construction which the company belives is neccessary to perform in accordance to transportation policy. The construction projects which are classified within this plan and are therefore agreed in the transportation policy. Payments are received according to a payment plan which is connected to the expected progress of the construction projects. Included in this part of the service aggreement is a management fee due to the projects. For the year 2010 this amount was ISK 32 million. In the same period the amount for construction projects were in total of ISK 387,8 million.

Service aggreements for operations

On the basis of the service aggreement with he Ministry of the Interior the Company provides navigation services in the local airspace. Operations, maintance and construction of airports and landing strips, as well as the operation of the Air Traffic School and publishes the AIP handbook.

The company is obliged to have in effect all legally binding insurance including liability insurance for air traffic control, airports and aircraft testing. The liability coverage of these insurances at year-end 2010 amounted to USD 500.000.000 for airports, USD 1.000.000.000 for air traffic control and USD 500.000.000 for flight testing.

All of the Company's insurance is exempt from liability because of acts of terrorism. The Company has taken out insurance against terrorism covering damage amounting to as much as USD 15.000.000.

Obligation due to employees

The Company has all employee insuranced in accordance with applicable collective agreements, except certificates of insurance for air traffic controllers. According to collective agreements, the Company shall at its own expense ensure certification of each controller that has VFR and/or IFR qualifications. The Company has not purchased insurance and therefore has an obligation in accordance with applicable collective agreements, if loss of certifications occurs.

24. Approval of financial statements

The financial statements were approved by the Board of directors and authorised for issue on 1 April 2011.

25. Consolidated ratios

From Statement of Comprehensive Income:	2010
Profitability	
Earnings before interests, taxes, depreciation and amortisation (EBITDA)	3.044.627.499
a) Contribution margin on operation	22%
b) Profit margin on operating revenue	15%
c) Earning per share (EPS)	0,38
d) Return on equity	23%

a) EBITDA/total revenue; b) Net income/total revenue
c) Earnings per share (EPS); d) Net income/average equity

From Balance sheet:	31.12.2010
Activity ratios	
e) Investment in inventories	0,03
f) Rate of return on assets	0,43
g) Inventory turnover	7,24
h) Receivables turnover	14,37

e) Inventory/revenues; g) Cost of goods sold/average inventory
f) Net income/average total assets; h) Reveneus/average accounts receivables

Liquidity ratios	
i) Quick or acid-test ratio	0,90
j) Current ratio	1,01

i) (Current assets - inventories)/average total assets; j) Current assets/current liabilities

Coverage ratios	
k) Equity ratio	0,32
l) Internal value of shares	1,84

k) Shareholders equity/total assets; l) Shareholders equity/capital stock

From Cash flow:	2010
m) Net cash debt coverage	0,07
n) Quality of sales	0,75
o) Quality of net profit	1,23

m) Cash flow from operat./Total liabilities; n) Paid in revenue/stated revenue
o) Cash flow from operat./net profit

Operating expenses as percentage of revenues	2010
Cost of goods sold/income from retail division	47,43%
Salaries and related expenses/operating revenues	43,82%
Administrative expenses/operating revenues	4,37%
Other operating expenses/operating revenues	12,57%
Depreciation and amortization/operating revenue	9,35%
Operating expenses/operating revenues	87,81%

ISAVIA
www.isavia.is
Tel: +354 424 4000
isavia@isavia.is